STUDIES IN PRACTICAL BANKING

BEING THE
GILBART LECTURES FOR 1932–1935

BY

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WITH A FOREWORD BY

BERNARD CAMPION

ONE OF HIS MAJESTY'S COUNSEL

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FOREWORD

THE author of this useful contribution to Banking Practice has done me the honour of inviting a foreword. I gladly accept the invitation, for Mr. Jones and I have had the task (each of us for several years in succession) of endeavouring to uphold the high tradition of the Gilbart Lectures on Banking under the direction of the authorities of King's College, University of London. Whatever may have been the verdict in my case, there can be no doubt as to the conspicuous success of Mr. Jones. I have not been able to peruse the book as it now stands, but I read the lectures delivered by Mr. Jones, as reported at the time, and can heartily commend them in their permanent form as embodied in these pages as a valuable and highly useful contribution to a wide and difficult subject.

It is a tribute to the wisdom of those responsible for selecting the Gilbart lecturer that they have included both lawyers and practical bankers in their list. The lawyer may not always appreciate the practical points that press the banker, nor express the operation of law with sufficient regard to the actual everyday operations of the banker. On the other hand, the practical man who is not a lawyer may, not infrequently, fail to apprehend truly the scope and exact effect of legal decisions; more especially as in the most important cases he is met with marked differences of opinion of the Judges themselves, both as to the facts, the proper inferences to be drawn from them, and as to the application of the law to the facts.

Mr. Jones naturally has brought to his task a close and intimate knowledge of banking practice and customs, and there speaks with authority. Since these practical matters are largely affected by legal decision, it was necessary

also that he should have a sound view of the decided cases. From my reading of his lectures I venture to say that in this respect he has shown a marked efficiency. It would not be expected that a mere lawyer should always agree with him—although I recall no serious disagreement—but it is a pleasure to bear testimony to his careful and discriminating understanding of the relevant cases.

With confidence I commend these STUDIES IN PRACTICAL BANKING to the banking world, and not only to bankers, but to accountants, auditors, company officials, and indeed to the business community as a whole. Everyone will find here a safe and informative guide to the matters treated by the author.

In congratulating Mr. Jones, I should like also to congratulate the publishers of this book, to whom we all owe so much for their enterprise in providing so many useful books by authoritative writers on the law and practice of banking. This little book will hold a high place in that series. Indeed, as a lawyer I feel that with these sources of information open to us, the mere lawyer ought no longer to plead too great an ignorance of banking in its purely practical aspect.

BERNARD CAMPION

PREFACE

TO THIRD EDITION

Opportunity has been taken in this third edition to bring up to date those matters relating to limited companies, following the passing of the Companies Act, 1948. Other matters requiring revision have had attention.

R. W. JONES

PREFACE

TO FIRST EDITION

Suggestions have come from various quarters that the usefulness of the Gilbart Lectures for the past four years would be enhanced if they were gathered together in book form and copiously indexed. This is the reason and excuse for the present volume, which reproduces the above lectures with such slight alterations necessary to bring the subject-matter up to date. The colloquial and direct method employed in the delivery of the lectures has been retained in the hope that it will make for clarity and stimulate interest in the subject-matter.

The quotations from Gilbart's works which prefaced each series of lectures have been retained, notwithstanding that they are of general purport and not necessarily relevant to the particular chapter they preface.

Acknowledgment is made to all those friends in the banking world who have placed their experience and knowledge at my disposal. Especially are my thanks due to my colleague, Mr. L. P. Galpin, for his invaluable help in preparing the lectures for press, in proof-reading, and in indexing.

R. W. JONES

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JOINT ACCOUNTS

"To be a good banker requires some intellectual and some moral qualifications. A banker need not be a man of talent, but he should be a man of wisdom. Talent, in the sense in which the word is ordinarily used, implies a strong development of some one faculty of the mind. Wisdom implies the due proportion of all the faculties. A banker need not be a poet or a philosopher—a man of science or of literature—an orator or a statesman. He need not possess any one remarkable quality by which he is distinguished from the rest of mankind. He will possibly be a better banker without any of these distinctions. It is only necessary that he should possess a large portion of that practical quality which is called common sense. Banking talent consists more in the union of a number of qualities, not in themselves individually of a striking character but rare only in their combination in the same person. It is a mistake to suppose that banking is such a routine employment that it requires neither knowledge nor skill. The number of banks that have failed within the last 50 years is sufficient to show that to be a good banker requires qualities as rare and as important as those which are necessary to attain eminence in any other pursuit."—*The Logic of Banking*, by J. W. Gilbart.

You will observe that the author suggests that common sense in a banker is to be preferred to more ornate qualities of mind, and I dare say you have all met colleagues of the old school who disparage the acquisition of any sort of technique in banking matters, protesting that common sense is the sole requisite for the practical banker. But you will note that later on in the passage above the author combats the notion that banking is a routine matter, demanding neither knowledge nor skill, and I wish to preface what I have to say by reminding you that the

practice of banking cannot be regarded as something apart from the law of banking. The practical banker does not deal with his daily problems solely from the viewpoint of common sense; experience, fortified by knowledge and theory, is a necessary part of his equipment, and to suggest that there is a great gulf fixed between practice and theory is specious and fallacious. In these days there is no room for this heresy, and I suggest that orthodox banking practice must be well grounded on the law relating to the subject—that the truly practical banker is he who has sufficient knowledge of the legal principles underlying the subject to know when to insist on the strict legal requirements of the case being carried out and when to waive them as a matter of expediency. The working banker cannot be expected to be a technical expert, although the Courts have occasionally thought otherwise, but he should have that modicum of knowledge that will enable him, when confronted with an unusual problem, to decide whether he can safely proceed in the light of his own experience, or whether he should call for competent legal advice.

To hand over a problem to the bank's solicitor without endeavouring to lay hold of the essential principles involved, to act blindly on a legal opinion without striving to appreciate the issues at stake—that is the attitude of mind that I call reprehensible.

We can view this matter from another standpoint, however. Not only is the practice of banking shaped in its development by the law of banking, but also the law on the subject is largely influenced by practice. For, after all, banking law is to a considerable degree found in the law merchant, which has been described by Professor Jenks as the general body of usages which grew up among persons engaged in commerce. This part of the common law is nothing more nor less than the judicial recognition by the Courts of the salutary practices of those engaged in commerce. It is the endowment with legal sanction

of those customs which the mercantile community has gradually adopted as being in the best interests of commerce generally. So we see that practice and law are complementary.

The bias of my treatment of certain types of accounts will be towards the practical aspect of the subject: but this, you will realise, involves the consideration of certain legal principles and the examination of various cases to which these principles have been applied by the Courts.

* * * *

We will consider, first of all, the joint account pure and simple—that is to say, the account conducted with two or more parties who are neither partners, nor executors, nor trustees.

It is obviously of the utmost importance to get the manner in which the account is to be conducted made plain at the outset, and this refers not only to withdrawals from the account, but also to all matters relating to securities, advances, bill transactions, and the like. A bare joint authority for either of two joint customers to sign on the account does not extend to withdrawals of articles lodged for safe custody, does not make one party responsible for an overdraft created by the other, and does not cover dealings with bills or securities.

The practice of bankers differs considerably as to the type of mandate taken on the opening of such an account. In some cases joint customers sign a comprehensive authority covering all possible banking operations on the account. In other cases a mandate is completed which has reference to credit accounts only, a separate agreement being executed if an advance is contemplated.

Again, arrangements for dealing with securities and articles left for safe custody may be included in the general form in some instances, and be the subject of a special authority in others.

However, whether one inclusive document is used, or

separate mandates are employed for different classes of transactions, it will be found that provision is usually made for the following matters and contingencies.

Drawings. Firstly, clear instructions will be taken as to the drawing of cheques—whether both, or either, or all, or some of the joint account holders may draw on the account. The ordinary rule regarding joint debts is that payment by a debtor to one of several joint creditors is a good discharge against all, provided that the debtor was unaware of any lack of authority on the part of the creditor in question. This, however, does not apply to the particular form of debt existing between banker and customer, for it is part of the law merchant that a banker, as a debtor of his joint customers, does not get a good discharge if he pays one of them without the mandate of the others.

"It is a general rule that a man may pay a debt to one of several persons with whom he has contracted jointly. In the case of a banker he cannot do so, but that arises from the particular contract which exists between him and his customer. It is part of the law merchant that bankers shall not pay to one of several jointly interested without the consent of the others, except by an express agreement." Maule, J., in *Husband* v. *Davis* (1851). If authority is given for the drawing of cheques by, say, either of two joint account holders, it must be remembered that any such occurrence as death, bankruptcy, or mental infirmity automatically revokes such authority.

While obviously a party authorised to sign may stop payment of his own cheque, it is also in order for the other party to the account to countermand payment of such a cheque, such a countermand operating as partial revocation of the general authority given for the drawer to sign.

Survivorship. Then reference is usually made in the mandate form to the question of survivorship. This is not so

much a covenant, or agreement, to the effect that any credit balance shall vest in the surviving parties, as an admission by the parties concerned that such is the law of devolution between joint owners. In the case of *In re Shields, Corbould Ellis* v. *Dales*, [1912] 1 Ch. 591, this principle was spoken of as an implied term of the contract between banker and customer as a result of practice. Strictly speaking, on proof of death of one of two joint customers, the survivor is free to deal with the balance, and the banker is under no duty either to seek out the personal representatives of the deceased or to pay heed to any claims they may make on the credit balance. The question whether both or either of the parties signed on the account is of no moment, for any such mandate is cancelled by death. It is customary to strike the name of the deceased out of the heading of the credit account, which is continued as a sole account, subject to what is said below.

This does not mean that the survivor necessarily gets an absolute and beneficial ownership in the balance—he merely is entitled to give the banker a good discharge for the balance. He will be accountable to the personal representatives of the deceased for that portion of the balance that belonged to the latter's estate. He holds such moneys as trustee for such estate—there is what is called a resulting trust.

It is the practice of bankers to supply such a party with a copy of an Inland Revenue memorandum addressed to the survivor, who is under a duty to furnish information concerning the ownership of the balance to the Estate Duty Office.

It is possible however that the executors of a deceased joint account holder may prefer a claim to the credit balance. A banker would in such a case recommend the personal representatives to apply to the Court for an injunction and meanwhile act warily before paying away any part of the balance to the survivor.

Husband and Wife. There is one type of joint account

where the above principles in regard to the question of benefit to survivor are not applicable. I refer to the very common instance of the joint account of husband and wife. If in such a case the husband predeceases his wife, the presumption of a resulting trust laid upon his widow is rebutted and the balance of the account will be regarded as an advancement in her favour. (*Foley* v. *Foley*, [1911] 1 I.R. 281.) The widow's claim to the balance might be defeated however by a direction in the husband's will or by arrangements made on opening the account. In *Marshall* v. *Crutwell* (1875), 20 Eq. 328, it was held that where the account was opened in joint form for the husband's convenience, it belonged to his estate and could not be claimed by the wife. Thus there is a special significance in the "benefit to survivor" clause in the mandate form for a joint account of husband and wife, for it settles the question of intention.

Additional Accounts. A carefully drawn mandate will make reference to the opening of more than one account or of a deposit account, for it is not settled whether a mandate to open a current account extends to opening further accounts of a current or deposit variety.

Joint Debts. Power to draw cheques does not of itself connote power to overdraw the account, and unless arrangements are made, one joint account holder will not be responsible fora debt created on the account by another. Accordingly, arrangements are generally made for power to create an overdraft to run side by side with power to draw cheques.

If borrowing arrangements are made on a joint account, it is of the utmost importance that several liability be established. Some banks incorporate this in the general form of mandate, while others provide for the matter in the shape of a separate agreement under hand, duly stamped. The advantages of joint and several liability over joint liability are so important that a little time may profitably be devoted to a consider-

ation of the differences between the two classes of liability.

With joint liability, a creditor can bring only one action and is debarred from successive actions. He need not, but should, sue all the debtors together, for if he sues one, or some, but not all, and obtains judgment, which is unsatisfied, he is debarred from suing the remainder. If joint and several liability is stipulated for, a creditor has as many rights of action as there are debtors; he can sue all together, or he can sue every one in succession until he has recouped himself with twenty shillings in the pound. An unsatisfied judgment against one debtor will not be a bar to an action against the others.

Secondly, with joint liability, the death of one debtor leaves the creditor with sole recourse against the survivor or survivors. Just as we have seen that the benefit of a debt due from a banker to joint customers passes to the survivors, so the liability for a debt due from joint customers to a banker rests solely on the survivors in the absence of other arrangements. If several liability has been covenanted for, the estate of a deceased joint customer can be held liable for the amount of the debt due at the time of his decease. If the account is then broken and a balance struck, recourse can be had against the assets of the deceased; if the account is not converted from a current account into a stopped account, the operation of the rule in *Clayton's* case will result in all payments-in being applied in reduction of the debt existing at the time of notice of the decease and all withdrawals being chargeable against the survivors only.

Let us take a concrete case. If A and B are jointly indebted to you on overdrawn account, the security being lodged by A, who subsequently dies, the position will then depend on whether the liability of A and B was joint only or joint and several. If no stipulation had been made for several liability, you can look only to B, the survivor,

for the amount of the overdraft. It has been suggested that if you hold adequate security lodged by the deceased you will possibly have no recourse against it, for the debt is no concern of his estate. It is the responsibility of the survivor alone. If the precaution had been taken to obtain an admission of joint and several liability on the part of A and B, the estate of A would be liable, and the security lodged by him could be utilised in repayment of the amount due at the time of A's death, provided that this had been determined by duly breaking the account. Some banks make assurance doubly sure by providing for such a contingency in the form of charge signed by A in respect of the security lodged by him. Not only is joint and several liability acknowledged, but such a form also recites that the security lodged is to be held as cover for all kinds of debts due alone or jointly, "including moneys owing from a survivor or survivors in joint account." If by any chance several liability had not been established in other form, this last phrase ensures that the security is available for the debt which, on the death of A, would otherwise have devolved solely on B.

The case law on this question of the sole liability of the survivors for a joint debt is not too clear. The case usually quoted in banking textbooks (*Other* v. *Iveson* (1855), 24 L.J.Ch. 654), refers to peculiar circumstances, where one party joined two others in a joint account, primarily in the nature of a surety, and on his decease his estate was held to be free from liability in respect of the joint indebtedness. An earlier case (*Thorne* v. *Jackson* (1837)) suggests that any debt contracted by two or more persons together is impliedly a matter of joint and several liability. Eminent authorities treat the matter as settled however. Thus Halsbury's *Laws of England*, Vol. VII, p. 357, states: "According to the Common Law, it is clear that on the death of one of the persons by whom a joint promise has been made, the liability devolves upon the survivors, and representatives of the deceased are under no liability."

Dr. Heber Hart and Sir John Paget are likewise of the same mind on the subject.

The third advantage of joint and several liability over joint liability is that whereas, in the latter case, no right to set-off accrues to the banker against any private accounts of the parties in respect of a debt on the joint account, in the former case the banker is entitled to set-off any credit balances on the private accounts against an overdraft on the joint account. It is not infrequent in practice for such overdrafts to be allowed in reliance on a substantial credit balance on the sole account of one of the parties, but in the absence of an agreement as to joint and several liability such reliance is illusory and ineffectual. Of course, any such right must not be used arbitrarily; while the accounts in question are running accounts, due notice should be given of any intention to set-off in the absence of an agreement to that effect.

The comprehensive form of mandate will also deal with the withdrawal of securities and articles left for safe custody. Powers may have been given for either of two parties to draw on the account, but this does not extend to withdrawing any lodgments of valuables or securities in the joint names. Express authority must be given in the mandate if either party is to deal with securities or articles lodged for safe custody.

In some mandates the question of pledging or charging security for advances is dealt with and powers may be given to one of two joint account holders duly to charge security for such a purpose. Possibly this would be efficacious in the case of stocks and shares held in the joint names in so far as it gave an equitable charge, but I suggest that such security, in the sole name of A, could not be validly charged by B by virtue of such mandate, for a power of attorney would be requisite in such a case. Most certainly title deeds of property held jointly could not be effectively charged by one of the two parties alone in the absence of a power of attorney. In practice, a

banker will get security in joint names charged by all the parties concerned.

Death of Joint Customer. Questions of practical importance generally arise in relation to joint accounts on the happening of such emergencies as death, bankruptcy, or insanity of one of the parties.

On receiving notice of the death of one of two joint customers, any cheques presented, signed by the deceased alone under authority, should be returned. If the cheque is signed by the survivor alone, in accordance with the mandate, it should, technically speaking, be returned; for such mandate is revoked by the death of one of the parties thereto. However, as normally the survivor is free to deal with the balance, the cheque could be safely paid and the survivor's confirmation obtained thereafter. It would be necessary, of course, to get formal proof of death exhibited. Any articles, such as a deed box, lodged for safe custody in the joint names, should not be handed to the survivor without the consent of the legal personal representatives of the deceased.

Bankruptcy of Joint Account Holder. The bankruptcy of a joint customer likewise cancels any mandate given as regards operations on the account, which should cease. The money on the account will, in due course, have to be apportioned between the solvent party and the trustee of the insolvent party according to the facts of the case. Any cheques drawn by the insolvent customer must be returned with the answer "Refer to drawer," and cheques drawn by the solvent party should likewise not be paid. It may be that the latter is drawing what properly belongs to him, but obviously the banker cannot determine this, and safety lies in paying only on the joint directions of the trustee and the solvent party. Care must be taken, of course, not to damage the latter's credit if you have to return his cheques, and the discreet answer given should make it plain that no aspersion is being cast on his credit. While most textbooks utter this warning,

few give a suitable form of answer in such a case, and I venture to suggest that "Joint account holder B in bankruptcy" might meet the case. If notice of a Receiving Order comes to hand in respect of a joint customer, you should stop operations on the account and inform the Official Receiver that, while the party is not a customer in his sole right, he is known to you in account with another party. You will shortly afterwards receive a request from the Receiver for any balance, but if the account is in credit you will first obtain the written authority of the solvent party before paying the money away. If any dispute arises, it must be settled between the parties concerned and you could interplead if necessary. If the account is in debit, you should inform the Receiver of the amount of the debit, giving the usual information as to any security, and await developments.

It is, possibly, hardly necessary to remind you that it is not merely a Receiving Order that will modify your attitude to a joint account, for notice of a bankruptcy petition against a joint customer will equally involve the cessation of operations on the account; and the commission of an act of bankruptcy on the part of a joint account holder, if it comes to your ears, will require caution on your part, in that any payments by the insolvent customer to third parties cannot be upheld against a trustee in bankruptcy. Any articles lodged by the insolvent customer for safe custody should not, of course, be delivered to him, but held to the order of the Official Receiver or Trustee in Bankruptcy. Furthermore, any joint lodgments should only be delivered against the joint authority of the solvent party and the trustee or Official Receiver.

The insanity of a joint customer countermands any authority given in respect of operations on the account, which should be stopped pending joint instructions from the sane party and the Receiver in Lunacy, if one is appointed.

If a garnishee order is served on a banker specifying a

judgment debtor who is only known to you in joint account with another, such account is not attached, and the solicitor acting for the judgment creditor should be advised of the position with a view to the withdrawal of the order. But a garnishee order specifying two judgment debtors will attach any balance standing in the name of one of them.

Sometimes a joint customer gives a power of attorney to an outside party. This power does not enable the attorney to operate on the joint account in place of the donor, unless the other parties to the account concur. If, of course, the joint account was that of trustees, no concurrence of the other parties would be necessary if the power was in respect of the donor's absence from this country for longer than one month, for Section 25 of the Trustee Act, 1925, expressly provides for this contingency.

CHAPTER II

PARTNERSHIPS

CLOSELY allied to joint accounts are the accounts of partnerships.

Operations on the current account of a firm are largely governed by the same conditions applicable to a joint account, and any special treatment only emerges when such matters as advances, the security for advances, insolvency, and negotiable instruments are concerned.

It will, I think, tend towards clearness if we consider first of all that part of the law relating to partnerships that is particularly applicable to banking matters and then proceed to examine its practical application. What I have to say now will relate to unlimited partnerships, a word being reserved later on for the comparatively rare class of limited partnerships.

The bulk of the law relating to the subject is codified in the Partnership Act of 1890, which defines a partnership as "the relation which subsists between persons carrying on a business in common with a view of profit." The law prescribes the minimum of formality in the setting up of this relationship; no registration is necessary, no written agreement or deed of partnership is requisite, though highly desirable; all that is necessary is some sort of agreement—written, oral, or implied—between the parties. A limitation is imposed by the Companies Act, 1948, on the number of partners—ten in the case of banking firms and twenty in other cases. Any larger association of individuals for business purposes requires incorporation under the Companies Act, 1948.

There is a disposition to regard a partnership, because it has a firm name, as an entity existing apart from its members. In Scotland this is so, for Section 4 (2) of the

Partnership Act provides that a Scottish firm is a legal person distinct from the partners of whom it is composed. But in England and Wales there is no such conception of a partnership, and the firm name is but a convenient abbreviation for the names of all the members of the firm.

Co-ownership. A distinction must be drawn between co-ownership and partnership, for the rights and liabilities attaching to the latter are vastly different from those belonging to the former. Joint tenancy, part ownership, the sharing of gross returns, do not necessarily connote partnership; the receipt of profits is *prima facie*, but not conclusive, evidence of the relationship. The criterion appears to be this: can there be construed from the association of the parties an intention to join together in carrying on business with a view to sharing profits? There are three broad distinctions between co-ownership and partnership which may help us to appreciate the point. Firstly, co-ownership is not necessarily the result of agreement, while partnership is; secondly, co-ownership does not necessarily involve working for a profit, while partnership does; thirdly, a co-owner has the right of free disposition over his property, while one partner cannot replace himself by another without the consent of his co-partners.

Liability of Partners. The importance of establishing whether a partnership relation exists between two or more parties will be appreciated when I draw your attention to the two dominant principles underlying the relationship. These are, firstly, the unlimited liability of each and every member of the firm for the firm's debts; and, secondly, the power of any partner to bind his co-partners in the ordinary course of partnership business, subject, of course, to any restrictions in the articles of partnership of which outside parties may be aware.

This unlimited liability means that every partner is liable for the firm's debts to the full extent of his private

resources in addition to his partnership capital; it means that every secret partner is fully liable whether the creditor was originally aware of his existence or not; and it means that any person who in any way holds himself out as a partner is fully liable for the firm's debts to the creditor who is thus misled. Incidentally, sleeping partners should no longer be secret partners if the provisions of the Registration of Business Names Act, 1916, are carried out, for this provides that the true surnames of all the partners must appear on the firm's notepaper, if not included in the firm name.

The liability of partners in England and Wales for debts and contracts is joint only, while in Scotland it is joint and several. This means that in England and Wales care must be taken to join all partners in an action, preferably by suing the firm in the firm name; for, as you will recollect, if this is not done, any unsatisfied judgment against those who are sued will effectively bar an action against any uncited partners. Thus in *Kendall* v. *Hamilton* (1879), 4 App. Cas. 504, two known partners were sued for a debt owing by the firm, and judgment was obtained, but it was only partially satisfied. Subsequently, the plaintiff Kendall discovered the existence of a sleeping partner of substantial means, named Hamilton, and thereupon commenced an action against him for the unsatisfied portion of the debt. The Court held that, the debt being a joint obligation only, the judgment obtained against the first two partners was an effective bar to an action against Hamilton.

There is, however, a modification of this principle of joint liability in that, on the death or bankruptcy of a partner, his responsibility for the partnership debts is not extinguished and his estate is severally liable. But you should note in this connection that partnership creditors are postponed to the creditors of the private estate, who must be paid in full from the private estate before any distribution is made in respect of the firm's debts.

Let us now consider the particular formalities and precautions which should be observed in conducting an account with a firm. If articles of partnership are produced, they should be scrutinised to find out, among other things, if any of the implied rights of the partners are restricted or modified, and if arrangements are made regarding operations on the banking account. If nothing is said about these matters any partner is entitled to draw cheques in the firm name, and by so doing he will bind the firm. The Bills of Exchange Act has something to say on this point in Section 23, which recites in Sub-section (2) that "the signature of the name of the firm is equivalent to the signature by the person so signing of the names of all persons liable as partners in the firm."

It is usual, however to take express instructions as to who may draw on the account and the form of signature to be employed. Some banks have a special form of mandate for the opening of partnership accounts, while others make use of the form of authority devised for joint accounts. But if no form of mandate is taken, a cheque signed in the firm name by any partner will be a good discharge to the bank against the firm in the absence of abnormal circumstances.

One partner has power to countermand the payment of cheques drawn by another. The question of the payment of cheques presented after notice of the death of a partner is not without complications. It does not depend on whether the cheque was drawn by the deceased partner, for his signature in the firm name is equivalent to the signature of all members of the firm. On the one hand, as the decease of a partner puts an end to the partnership as such, the authority of any one partner as agent for the firm is revoked, and on these grounds it would seem that such cheques should not be paid. On the other hand, the surviving partners can deal with the account for the purpose of winding up the firm, and could consequently confirm any cheques outstanding at the time of decease.

Fiduciary Relationship of Partner. Transactions on the private account of a partner require scrutiny in certain circumstances. Cheques payable to a firm should not be accepted for the private account of a partner without inquiry being made of the other partners. Failure to query such a transaction would certainly deprive a banker of the protection of Section 82 of the Bills of Exchange Act on the ground of negligence. I have, possibly, no need to remind you of the numerous cases where the wrongful dealing by an agent with a cheque payable to his principal, or by a person acting in a fiduciary capacity, has put the collecting banker outside the protective pale of Section 82. If a partner pays to the credit of his private account a cheque drawn by him on the firm's account there is no *prima facie* case for inquiry—the transaction may represent repayment of a loan to the firm, or a share of partnership profits. In *Backhouse* v. *Charlton* (1878), 8 Ch.D. 444, transfers of this description were held to be regular on the face of them. I suggest, however, that the particular circumstances, such as the standing of the partner and the amount of the cheque, would influence the banker in dealing with the situation. But there is one clear case which would call for caution—where a banker has been pressing for reduction or repayment of a private overdraft, and the partner responds by offering for his credit a cheque drawn by him on the partnership account. This is on all fours with the fraudulent trustee liquidating his overdraft under pressure by a transfer from trust funds.

A banker is sometimes faced with an awkward situation when a sole trader offers cheques for collection ostensibly payable to a firm, and states that he is trading under that name. It is a vital matter to verify his explanation, and you will recollect that lack of proper confirmation was one of the counts against the collecting banker in *Guardians of St. John, Hampstead* v. *Barclays Bank, Ltd* (1923), 39 T.L.R., 229. In this case a new customer, calling

himself D. Stewart, paid in orders for payment of money made out to D. Stewart and Co., which orders were accepted for collection, on his assurance that he was trading in that name, without any further inquiry. To what lengths a banker should go to satisfy himself as to the regularity of the transaction it is difficult to say, but I suggest that a request to the customer for his certificate of registration under the Registration of Business' Names Act, 1916, might have salutary effect. The Act provides for the registration of every trading name where it is not the true surname of the trader. Some people think that this measure is a dead letter, but there is an average of 21,550 registrations yearly and, during the years 1937 to 1942, 196 prosecutions were instituted for failure to register.

One partner is entitled to open an account for the firm's business provided that he opens it in the firm name, although it is the practice to obtain the authority of all the partners. In the case of *Alliance Bank* v. *Kearsley*, two brothers carried on a coach-building business under the style of George Kearsley and Co., with two branches, one at York and one at Manchester. The partner in charge of the Manchester branch opened an account with the Alliance Bank for the firm's business in his own name. When the bank subsequently sued both partners for the amount of an overdraft, it was held that the other partner was not liable, as it was not in the ordinary course of business for one partner to open a firm account in his own name unless the other partner expressly or impliedly agreed to such a course.

It is a sound practice, when dealing with trading customers who borrow, to ask for a copy of the latest balance sheet. Not only does this help you to decide if the borrowing is commensurate with the size of the business and to estimate the probability of reductions from business profits, but it is helpful in detecting any irregularity in

the style of the account. You may be dealing ostensibly with a sole trader in whose name the account stands, and an examination of the balance sheet may disclose partnership capital, necessitating changing the account into the name of the firm and taking the instructions of the remaining members of the partnership.

As regards borrowing and bill transactions, a partner's authority depends on whether the firm is a trading or non-trading partnership, and the natural question here arises as to what is the distinction between the two classes. There is no answer to this query in the shape of a statutory distinction. A trading business has been defined as one which depends on the buying and selling of goods (*Higgins* v. *Beauchamp*, [1914] 3 K.B. 1192), and this must be the criterion applied in each case. Thus professional partnerships, such as doctors, solicitors, and accountants, are non-trading firms, and in decided cases the businesses of farmers and innkeepers have been held to be non-trading partnerships.

In a trading firm any partner, unless prohibited by the terms of the partnership agreement, has actual authority to pledge and sell the assets of the firm, to contract debts, to borrow and to draw, accept, endorse, and discount bills of exchange. In a non-trading firm, no such authority exists as regards borrowing, pledging partnership assets or indulging in bill transactions on behalf of the firm. It is well settled, however, that a partner in a non-trading firm can bind the firm by drawing cheques (*Backhouse* v. *Charlton* (1878), 8 Ch.D. 444).

In practice, express authority is taken from the members of the firm—be it trading or non-trading—as to the method by which advances are to be negotiated, partnership assets pledged, and bill transactions effected. But I suggest that a banker must use a certain amount of caution in permitting operations on the account by one partner, even though such partner is acting under authority, for such authority is only referable to those

acts done by the partner which are connected with the firm's ordinary course of business.

This doctrine might press very hardly on a banker, but partners who sought to avoid liability for a cheque drawn by their co-partner for non-partnership purposes would have a hard job to establish the banker's knowledge of such irregularity. The evidence would have to be of a very definite and conclusive character. There would have to be some knowledge on the banker's part of the circumstances surrounding the drawing of the cheque in order to fix him with liability.

In a Scottish case (*Clydesdale Bank* v. *Continental Chocolate Company* (1915)) two out of three partners repudiated liability for a cheque drawn by the other on the ground that it was drawn for a purpose apparently unconnected with partnership business, and that the bank was aware of this. It was held that the bank had not sufficient knowledge of the transaction to put them on notice.

We have seen that in England and Wales partnership liability is joint only, and it is very desirable to get the members of a borrowing firm to covenant for several liability. Among other advantages, it will mean that a banker's position in the administration of a deceased partner's estate will be improved, for he will not have to wait until the private creditors of the deceased have been satisfied, but can claim side by side with them for any debt due by the firm.

Furthermore, such a provision will give a banker a right of set-off on any private account of a partner in respect of the firm's debt, and in the event of bankruptcy he will have a right of double proof, for a joint and separate creditor may prove concurrently on the joint estate and the separate estate, his redress being limited, of course, to twenty shillings in the pound.

As regards the pledging or mortgaging of security for advances, it is the usual practice to get all members of the

firm to execute the necessary documents. One partner could, in a trading firm, validly pledge negotiable instruments and also execute a memorandum of deposit over the deeds of partnership property. He could not give a legal mortgage over such property, for one partner cannot bind the firm by deed, unless authorised so to act, in which case the authority itself would have to be by deed.

A legal mortgage given by one partner in the absence of proper authority would not be wholly void; it could be treated as an equitable charge, for in transactions where a deed is not necessary the seal may be disregarded and the signature considered as applying to a document under hand. Thus in *Marchant* v. *Morton Down & Co.*, [1901] 2 K.B. 829, one partner sought to make a legal assignment of the firm's debts under seal. It was held that, while he had no power to bind the firm by deed, his signature to the document would be construed as the execution of an equitable assignment under hand.

When title deeds of property are offered as security they may be in the sole name of one partner or in the names of all the partners jointly. In the first instance the property in question may belong to one partner in his own right, the firm having a tenancy thereof, or it may be held by him in trust for the partnership, in which case all the partners should join in the execution of any charge or give an authority for him to mortgage it.

When scrutinising a partnership balance sheet you should query the inclusion, among the assets, of property charged by one partner ostensibly in his own right. In such a case the partner clearly holds it in trust for the firm, and you should regard it as direct and not collateral security, getting the confirmation of the remaining partners, as I have just pointed out. Where the property is vested in all the partners jointly,* it may be partnership

* If there are more than four partners, such property cannot, since 1st January, 1926, be vested in more than four of them, who will hold it in trust for all the members of the firm.

property or not, according to whether it has been treated as part of the firm's assets or not.

In either case the mortgage of the property will require to be executed by all, for it will be vested in the several parties on trust for sale specifying that they hold the property for themselves as tenants in common in equity or jointly as partners.

Incidentally, when searching the Land Charges Register, or other appropriate register, in respect of partnership property, searches should be made against the names of all the partners, as well as against the firm name, one reason being that, in the event of the firm's bankruptcy, a receiving order will have been made against each and every member of the firm and will be so registered.

Sometimes a guarantee of one partner, or a joint and several guarantee of all the partners, is taken in respect of a borrowing by the firm. Inasmuch as all the partners are already unlimitedly liable for the firm's debts, such a guarantee appears at first sight to be superfluous, but it has the merit of giving the banker a right of proof against the private estate of each guaranteeing partner without waiting until the private creditors are satisfied. If joint and several liability has been established, however, the same right of proof accrues, so that in such a case a guarantee has no practical advantage.

In some quarters it is considered that the taking of a guarantee brings home to the partners a sense of their personal liability for the firm's debts; on the other hand, it is as well to inform them that the amount of the guarantee is not the limit of their responsibility, and does not free them from liability for any borrowing in excess of the amount specified in the document.

Occasionally the guarantee of a firm is offered to secure the debt of a third party, and in such a case the signatures of all the partners should be taken to a joint and several guarantee, for one partner cannot, in the absence of

specific authority, bind his co-partners by executing a guarantee in the firm name.

Dissolution of Partnership. There now fall to be considered the cases where the partnership relation is severed, and this occurs on the retirement, death, or bankruptcy of one partner as well as in those cases where a dissolution of the firm takes place by agreement or order of the Court or the bankruptcy of the firm itself.

If the members of a firm decide to wind up the business, or if the Court decrees a dissolution, the partners' authority to bind the firm continues in so far as its exercise is necessary to wind up the business; if the members of the firm are at loggerheads and resort is made to the Courts, it is not infrequent for the winding-up to be put into the hands of a receiver. In such a case a credit balance on the firm's account can safely be paid over to the receiver after due confirmation of his appointment.

A partner's powers as agent for the firm then cease, for the trading activities of the firm are terminated, and the receiver's function is to realise the partnership assets, pay out the firm's creditors, and distribute any surplus among the partners, in accordance with the terms of the articles, if any. Occasionally a manager is appointed by the Court, and his powers are wider than those of a receiver, for he is empowered to carry on the business for the time being, to fulfil existing contracts, and to enter into such new contracts as are essential to the ordinary conduct of the business.

In this case also the Court appointment of a manager will be sufficient mandate to the banker to recognise his authority to deal with the firm's balance. Any borrowings that may be allowed on the account of a manager or receiver are his personal responsibility, and he cannot validly charge any assets of the firm as security without the leave of the Court.

Such examples of dissolution are comparatively infrequent, as compared with the cases where dissolution

automatically takes place by the retirement, death, or bankruptcy of one partner. It must never be forgotten that any change in the membership of a firm occasioned by the withdrawal, decease, or insolvency of a partner virtually puts an end to the firm; the surviving or remaining partners may continue to trade under the firm name, but, in fact, a new firm is created if they carry on for any purpose other than to wind up the affairs of the old firm.

Retirement of Partner. In the case of the retirement of a partner he will be liable for advances subsequently made to the firm unless the firm's bankers are notified of the severance of his relations with his co-partners, for Section 36 of the Partnership Act decrees that "where a person deals with a firm after a change in its constitution, he is entitled to treat all apparent members of the old firm as still being members of the firm until he has notice of the change." A secret partner could not be saddled with any liability for the firm's indebtedness incurred after his retirement, even though he omitted to notify the bank, for the equitable reason that credit was given to the firm without knowledge of or reliance on his membership thereof.

On notification of the retirement of a partner the banker's action will depend on several circumstances.

If the account is in debit, and security of the retiring partner is held, the account should be broken in order to establish the banker's right over the security for the debt existing at the date of notification of retirement.

If the security consists of partnership assets, such as the deeds of property jointly charged, the banker can continue the account for the time being, as the presumption is that the remaining partners are carrying on the business for the purpose of winding it up. If the retirement of one partner is accompanied by the admission of a new partner, a conveyance of the property is sometimes executed by the old firm in favour of the new firm, and this will entail the charging of the security anew.

In such a case it is advisable to break the old account and start afresh, a cheque being drawn on the new account for the amount of the old debt by all members of the firm, including the new partner, for an incoming partner is not necessarily liable for the debts of the old firm. If a separate conveyance of the partnership property is not made, the incoming partner should endorse the old form of charge to the effect that he agrees that the security covered thereby shall be available for the debts of the new firm as well as the old.

Death of Partner. The death of a partner likewise has the legal effect of dissolving the firm. The personal representatives of the deceased have no power to step into the dead partner's shoes—they cannot take any part in the management of the firm, and their sole concern is to see that a proper account is taken of what is due to the estate they are administering.

In the case of a credit account, there appears to be no reason why the account should not be continued unbroken by the surviving partners. In *Backhouse* v. *Charlton* (1878), 8 Ch.D. 444, it was held that where a banker had no notice of the state of accounts between the deceased partner and the survivor, he was under no duty to inquire. The banker is entitled to presume, in the absence of anything to the contrary, that the survivors will account to the representatives of the deceased for his share of the assets.

In the case where the firm is indebted to the bank, any action will depend on the nature of the security lodged. If it was charged by the deceased as his private property, or if you wish to retain a hold on his private estate, the account must be stopped in order to fix the liability of his estate, for otherwise all sums credited after the crucial date will go in the reduction of the liability, while all fresh debits will not be covered by the security held.

If the security held is partnership property, the account can be continued unbroken for the time being, for the

surviving partners are entitled to deal with the firm's assets so far as may be necessary to wind up the partnership business.

If the account is continued for an indefinite period, however, the presumption will be that it relates to a new firm the members of which will be liable for the share of the deceased partner in the old firm's assets. (See Section 43 Partnership Act, 1890.)

The power of the surviving partners in a firm to continue the partnership business in so far as it is compatible with the winding up of the firm, is illustrated, as far as banking operations are concerned, by the case of *In re Bourne, Bourne* v. *Bourne*, [1906] 2 Ch. 427. Here an overdrawn banking account of a firm was continued unbroken after the death of one of the two partners, named Grove, and the survivor, Bourne, at a later date gave the bank an equitable charge on the deeds of real estate which formed part of the partnership assets.

On the death of Bourne the mortgaged property was sold and the bank's right to appropriate as much of the proceeds of sale as was necessary to satisfy its debt was disputed by the executors of the partner first deceased. In the lower Court the bank's claim was upheld, and the decision was confirmed on appeal. The executors of Grove claimed that Bourne had no right to mortgage the partnership property after the death of Grove, and contended that the payments into the account after his decease and before the mortgage of the property was given had extinguished the original debt, and that by the working of the rule in *Clayton's* case the debt remaining at the time of Bourne's death was a subsequent creation, which could not be effectively secured by the mortgage of partnership property.

The Appeal Court made it plain that it is both the right and duty of a surviving partner to realise the firm's assets, and in giving effect to this duty he can validly mortgage partnership property. In this case the bank was entitled

to assume that the overdraft was a partnership matter in the absence of anything showing to the contrary, and hence the account was properly continued on an unbroken basis, and payments in could be appropriated to payments out right up to the time when matters were crystallised by the death of the surviving partner.

From the report of this case (which is available in the second volume of *Legal Decisions Affecting Bankers*, page 107) it can be inferred however, that if a banker is fixed with notice that a surviving partner is continuing the business for his own ends and not for the purpose of winding up the firm, any charge given by him over partnership assets would be subject to the rights of the estate of the deceased partner.

Bankruptcy of Partner. A third cause of dissolution of a firm is found in the bankruptcy of one of the partners. In such a case his authority to act on behalf of the firm, including powers to operate on the banking account, at once ceases and his estate will not be liable for the debts contracted thereafter by the solvent partners. Such partners are entitled to continue the business for the purpose of winding up, to get in the assets, and to complete transactions unfinished at the time of dissolution.

They may continue to operate on the banking account to this end and payment of cheques drawn by them will be a good discharge against the firm and the trustee. Neither the trustee in bankruptcy nor the insolvent partner has any power to deal with the partnership affairs, and the trustee's interest in the business lies in getting an account of the partnership business taken with a view to receiving the bankrupt's share therein.

A cheque presented signed by a partner known to have committed an act of bankruptcy should not be paid until confirmation of the other partners is obtained.

If there is a credit balance on the account of a firm, a member of which has become bankrupt, it can safely be paid to the solvent partners; theirs is the responsibility

to account to the trustee for the bankrupt's share in the firm's assets. If the firm is in debt to the bank and it is desired to retain any rights on the bankrupt's estate, it is necessary to break the firm's account.

If several liability is not established, the bank will be postponed in proving on the partner's private estate until all his separate creditors have been paid in full, which may mean that there will be nothing to come by way of dividend. If, on the other hand, several liability has been stipulated for on the firm's account, the banker can prove as a creditor on equal footing with the partner's private creditors. In either case there is no need to deduct the value of any partnership security before proving against the private estate of the bankrupt partner.

Bankruptcy of Firm. The last case of dissolution which we must consider is where the partnership itself becomes bankrupt. On such a happening the authority of the several partners to act for the firm ceases and the business vests in the trustee in bankruptcy in order to be wound up. Inasmuch as the title of the trustee relates back to the earliest of the acts of bankruptcy committed during the three months preceding the presentation of the bankruptcy petition, any transactions with the firm since that time are void as against the trustee, unless covered by Section 45 or Section 46 of the Bankruptcy Act, 1914.

With regard to operations on the banking account, any payments out after the receipt of notice of a petition, or after the date of (not notice of) a Receiving Order will be void against the trustee, and consequently any cheques should be returned with an appropriate answer. If any such cheques are paid in ignorance of a petition and of a Receiving Order on account of a delay in the advertisement of the latter, there is a slender relief afforded by Section 4 of the Bankruptcy (Amendment) Act, 1926.

After notice of the commission of an act of bankruptcy

by a firm, cheques should only be paid to the firm or its assignee. Cheques payable to a third party could not be upheld against the trustee.

If you happen to keep the private accounts of any of the partners, you must not forget that the bankruptcy of the firm involves the bankruptcy of the individual partners, and any steps you take with regard to the firm's account are equally applicable to the private accounts.

Proof in Bankruptcy. The dominant principle in the administration of the respective estates is that the firm's debts are payable in the first instance out of the partnership assets, and the private debts of the partners from their private assets. If a surplus results from any of the separate estates of the partners, it must be brought into the joint estate of the firm; and if a surplus accrues on the joint estate it is appropriated to the respective separate estates of the partners in due proportion.

There is an exception to the rule of keeping the joint and the separate estates distinct in the first instance, and it is this: if there is no joint estate on account of a total lack of assets, or because all the firm's assets are mortgaged with no available equity, the partnership creditors can prove on an equal footing with the creditors of the partners' separate private estates.

If you hold partnership securities which you do not propose to renounce or realise forthwith, you must assess their value before proving; if the security is collateral, in the sense that it is lodged by a partner as a private asset, you are, of course, entitled to prove for the entire debt of the firm, and to realise the partner's security without diminishing your claim against the firm's estate.

If you have taken the precaution to establish several liability and thus have a right of double proof and the security is partnership property, you should prove against the private estates for the whole debt without regard to the security and against the firm's estate after allowing for the value of the security.

If, on the other hand, the security is the private property of a partner, i.e. collateral, proof for the full amount can be made against the firm's estate, ignoring the security, the proof against the particular partner's estate being decreased by the assessed value of the security.

One further and final point in this somewhat complicated subject. You may hold security available for the debt not only of the firm but of an individual partner. In such a case, you can appropriate this security to whichever of the two estates you choose, and then proceed on the lines just indicated. Before making any allocation, however, you will be wise to study the statement of affairs of the respective estates in order to see the prospects of dividends.

As a general principle, it will be of advantage to allocate the security (which may be, remember, partnership property lodged to secure both the firm's and the partner's debts, or the partner's own property covering the firm's advance as well as his own) to the estate to which it does not belong, because such a course will mean that you will not have to account for the value of the security in respect of either debt, treating it simply on a collateral basis.

A point that is sometimes not appreciated arises in such a case as this: A and B are in partnership, and the firm's account is overdrawn against security deposited by A. Such security will, of course, be regarded as collateral or third party cover in the event of the bankruptcy of the firm, giving you recourse against its assets before dealing with the security. B dies, and the form of your charge permits you to continue the account with A against the same security. Your position will be different, for your security is direct and its value must be assessed and deducted from your proof in bankruptcy—you have lost your collateral ranking, and may prefer to break the account.

Insanity of Partner. It may happen that a member of a

firm becomes insane. Such an infirmity does not operate, like death, as a dissolution of the firm, but by Section 35 of the Partnership Act it is a ground for petitioning the Court for a dissolution. The Court's intervention may be sought by a co-partner or by the patient's committee, if one has been appointed, or by his next friend, or by anyone having a title to move in the matter.

It is necessary, of course, for the partner to have been found insane by inquisition—a very rare method—or to have been proved to be of unsound mind to the satisfaction of the Court. Apart from these steps, by the Lunacy Act, 1890, power is given to a lunacy Judge to dissolve a partnership when a partner becomes of unsound mind.

It is not a remote possibility that a partner who is insane may consider himself the only sane member of the firm, and, unless restrained, any contracts entered into by him will bind the firm if the other party to the contract is not aware of his disability. Thus, pending an action for dissolution, such an unfortunate may do considerable damage to the firm's business, and the remedy lies in an application for an injunction restraining the insane partner from meddling in the firm's affairs.

Limited Partnership. Finally, it is necessary for us to look briefly at the principal characteristics of a limited partnership. This type of firm was first made possible by the Limited Partnerships Act, 1907. You will appreciate that the idea has not appealed to the business community when I say that since the passing of the Act only 1426 such partnerships had been registered by the end of 1937.

To constitute such a firm there must be at least one general partner—fully liable for the debts of the firm—and one limited partner, whose liability is limited to the amount of capital put up by him, a withdrawal of any part of such capital rendering him liable for the firm's debts up to such amount.

These partnerships require registration with the Registrar of Companies, giving, among other things, details of

the amount contributed by the limited partner. The register is open to public inspection, and such access is useful if you wish to ascertain if a member of a firm, known to be a man of means, is a limited partner, for you may be proposing to extend accommodation to a firm in reliance on the standing of one partner. If it turns out that he is a limited partner, your reliance on his unlimited liability for the firm's advance will be in vain.

A limited partner must not take part in the management of the partnership business under pain of incurring liability as a general partner while so acting. According to Section 6 of the Act, he may inspect the firm's books, inquire into the state and prospects of the business and advise the partners thereon, and this gives rise to the natural question—can he demand information from the firm's bankers concerning the state of the partnership account? The section in question provides no clear answer to this query, and I suggest that the directions of the general partners should be taken as to the degree of information that should be afforded to him.

One thing is certain—a limited partner has no power to draw cheques on the firm's account. The death or bankruptcy of a limited partner does not operate as a dissolution of the firm, and if dissolution does take place for any reason, the duty of winding up the business devolves on the general partners.

The Limited Partnerships Act provided for the winding up of an insolvent limited partnership under the Companies Acts, but the Bankruptcy Act, 1914, provides for the alternative method of winding up under the bankruptcy rules. A limited partner is necessarily not liable for any contribution beyond the amount of capital he has agreed to put into the firm, and he will be entitled to prove for a share of any surplus assets after the firm's liabilities have been met, his claim being in proportion to his share of the partnership capital.

CHAPTER III

COMPANIES

THE law relating to this legal person is different from the law relating to the human person. In the main, the latter is inhibitive, saying what you shall *not* do; but the law relating to the legal person—the company—is permissive—it lays down what the company *may* do, and anything done outside the pale of this legal sanction is beyond the company's powers.

A joint stock company is begotten and born of statute, its whole life is governed by statute, and it comes to an end in like manner as it began—by legal process. It is a legal person, enjoying a good many of the attributes of personality, and has an existence apart from its members; it is a separate entity, not to be confused with its shareholders, who cannot in the ordinary course of things be saddled with its liabilities over and above the amount unpaid in respect of the shares held by them.

It is the fashion to speak of certain private limited companies as "one-man" companies. This is an unfortunate term, for there must be at least two members of a private company; it is a specious phrase, for it suggests that the identity of the human person and the legal person can be merged, that transactions on the accounts of Mr. X and X and Co. Ltd. can be mixed with impunity.

The falsity of this notion has often been demonstrated at the banker's expense, and the pages of *Legal Decisions Affecting Bankers* are littered with instances of the danger of regarding the legal person—the company—as identical with the human person—its director. In such cases trouble has come from the creditors of the company—usually represented by the liquidator—who have challenged any payments to the credit of the directors' accounts which should have properly found a home in the company's account.

In like manner any liability incurred by the company cannot usually be laid at the door of the directors, for once the company has acquired a legal existence it can incur debts in its own name and bind itself by contracts on which it can sue and be sued as a legal person. The celebrated case of *Salomon* v. *Salomon and Co. Ltd.*, [1897] A.C. 22, reported in Vol. I of *Legal Decisions Affecting Bankers*, is worth studying on this point.

Opening of Company Account. I will first of all remind you of the formalities attendant on the opening of a company's banking account. Firstly, it is necessary to satisfy yourself that you are dealing with a properly incorporated company, that it is legally born, that it has acquired an existence apart from its members. In other words, you want to see its birth certificate, technically known as the certificate of incorporation. Once this has been issued by the Registrar of Companies there can be no gainsaying the existence of the company, no challenging the regularity of its incorporation

The next documents to inspect are the memorandum and articles of association. Although a banker is mainly concerned with these when a question of borrowing arises, there are certain matters to be looked at when banking relations are first begun. Firstly, in the case of a company already established you should get the copy handed to you confirmed as being up to date, for both the memorandum and the articles are capable of alteration after certain formalities are observed.

For example, touching the memorandum, the legal name of the company can be changed by special resolution and the approval of the Board of Trade; the objects of the company can be altered by a special resolution, and the capital can be increased by an ordinary resolution. Any of the articles can be altered by special resolution, and as the articles are particularly concerned with the powers and activities of the directors, you will appreciate

the importance of being in possession of up-to-date information on these matters.

If you are in any doubt, the plain and simple course is open to you to search the company's file at Bush House to see if any special resolutions have been filed that in any way alter the articles. In the case of a new company, you should scrutinise the articles to see if the first directors of the company are named therein. Likewise, you should ascertain if the articles name the bankers of the company. It is the exception, however, to find these two matters dealt with therein.

Usually, the first directors of the company are appointed by the subscribers to the memorandum under proper resolution (*vide* Table A, Clause 75), and you should accordingly get a certified copy of this resolution and see that any changes in the directorate or other officials of the company are notified to you in a similar way. Whether the company is newly incorporated or not, you must get a certified copy of the resolution of the Board appointing you as banker of the company, and, usually, there is incorporated therein explicit instructions as to who shall draw cheques, draw, accept and endorse bills and deal with securities and safe custodies.

In the case of a public company, one further document should be produced before operations are allowed on the account—the certificate of authority to commence business issued by the Registrar when the company has issued a prospectus, or filed a statement in lieu of prospectus, and the secretary of the company has made a statutory declaration that an allotment of shares has been made to the amount of the minimum subscription and that the directors have paid the application and allotment moneys on the shares they have contracted to take up. Until this certificate is issued a public company has no power to contract or borrow.

Special Associations and Companies Limited by Guarantee. You will sometimes find that an association, or

society, or institution that banks with you has taken advantage of Section 19 (1) of the Companies Act, 1948, to register itself under the Act with limited liability, under licence from the Board of Trade to omit the word limited from its title. The advantages of such a procedure are that the institution or society has perpetual succession regardless of any change in its membership, its officers and members escape personal liability for its debts, and it can hold property in its own right, thus avoiding the vesting of its assets in trustees.

This method of incorporation is permissible where the association, etc., is formed for the promotion of commerce, art, science, religion, charity, or any other useful object, any profits or income being used in furthering its aims and not distributed by way of dividend to its members. In particular, you will find that many educational undertakings have been incorporated in this fashion.

Such a body need not include the word "limited" as part of its name, it rarely uses the word "company" in its title, and its governing body is often styled the "committee" or the "council" instead of the board of directors. Hence you may possibly overlook the fact that you are dealing with an incorporated body subject to most of the legal liabilities of a limited company other than the use of the word "limited" in its title.

When such a type of account is opened the ordinary formalities must be observed, as in the case of an ordinary limited company; the memorandum and articles must be perused and the certificate of incorporation exhibited. Usually the concern is registered as a company limited by guarantee, its members undertaking to contribute a specified sum—usually a nominal one—in the event of the company being wound up.

The fact that it is a public company will not involve getting a commencing certificate if the liability is limited by guarantee and not by shares, for such certificate only

applies to public companies with a share capital. If any advance is contemplated, the question of the company's powers to borrow and any limitations on the use of such powers by the governing body will require attention. Likewise any security of a registrable type will require registration at Bush House.

Private Companies. Probably among your company customers private companies predominate, for one of the principal features of modern commerce is the increasing tendency for sole traders and firms to convert their businesses into private limited companies, and the great majority of companies now registered at Bush House are private ones.

The principal inducement is, of course, the advantage of limited liability compared with the far-reaching financial responsibilities attaching to partners in a firm. Then the power of one partner to bind his co-partners while engaged in the firm's business—sometimes with devastating results—is exchanged for an arrangement whereby not only is the liability of members limited, but the powers of the directors are limited by the company's articles. Partnership deeds, however detailed and precise in their terms, frequently entail arbitration when partners are at loggerheads; in the case of a company the removal of directors for misconduct is a straightforward matter provided for in the articles.

We have seen that the death, bankruptcy, or retirement of a partner involves the dissolution of a firm, with its possible difficulties and embarrassment for the remaining partners. With a company you have unbroken continuity, despite the death, bankruptcy, or retirement of any of its members. With a partnership, changes by retirement or death involve the re-vesting of the partnership assets in the new firm; with a company there is a single ownership of its property undisturbed by change in membership.

In the matter of deed contracts, a company can be bound by the signing and sealing being effected by duly

authorised officials; in a partnership the co-operation of all partners is necessary in order to bind the firm by deed. Finally, the facilities given to a company to charge its fixed and floating assets by way of debenture make borrowing a simple matter; this procedure is not practicable with a partnership which, apart from mortgaging its fixed assets, cannot usefully raise money on the security of its stock-in-trade.

You will find that, while the owners of private businesses are generally alive to the protections and immunities enjoyed by a limited company, they are not equally sensible of the corresponding responsibilities that run with incorporation.

For example, a banker may readily grant occasional and seasonal unsecured accommodation to a sole trader or a firm, well knowing the standing and means of the parties concerned, who are personally responsible for the bank advance; if in due course the business is reconstructed as a limited company, a suggestion of a personal guarantee of the directors for similar accommodation is often ill received, and it is sometimes difficult to make the parties realise that the directors of a company are not legally responsible for its debts, as are the members of a firm for partnership debts.

Furthermore, your request for such documents as the memorandum and articles of association and the annual balance-sheet, and insistence on such formalities as resolutions *re* signing powers and borrowing sometimes give offence to old customers who have envisaged all the merits of limited liability without contemplating the duties and formalities that run with it.

A private company has three distinguishing features, according to Section 28 of the Companies Act, 1948. Firstly, it restricts the right to transfer its shares. It is not necessary for the restriction inserted in the articles to be express in form, a general discretion to the directors, to decline to register any transfer which

they do not approve, being sufficient. Such a restriction on transfer must apply to all classes of the company's shares.

Secondly, a private company limits the number of its members to fifty, exclusive of past and present employees. It is probably the exception to find a private company with a membership of anything like fifty, apart from its employees.

While there is a legal maximum as regards the membership of a private company, there is also a legal minimum, for Section 31 provides that if the number is reduced below two, and the business of the company is carried on for more than six months, the remaining member will be liable for the whole of the company's debts contracted after the six months. Furthermore, Section 222 makes such a reduction a cause of winding up by the Court.

Thirdly, a private company is prohibited from inviting the public to subscribe for shares or debentures. This in no way restricts the company in inviting existing members and debenture holders to subscribe for further shares and debentures. A private company that converts itself into a public company does not require a commencing certificate. A public company may convert itself into a private company by making the necessary alterations in its articles by means of a special resolution.

Certain privileges and exemptions enjoyed by a private company require noting.

Sundry formalities are waived with regard to its inception. The registration of the memorandum and articles of association will be followed by the issue of the certificate of incorporation, and the company can commence business forthwith without the necessity for a certificate of authority to commence business (Section 109 (7) (*a*)).

A public company must have a minimum of two directors, while a private company can function with one; in such case the sole director cannot also function as secretary to the company.

One of the most prized privileges of a private company used to be exemption from the filing of its annual accounts with its yearly return to the Registrar of Companies.

The Companies Act of 1948 now reserves this privilege for companies that really are private—the family type. Such concerns are to be known as "exempt" private companies; a private company not within this category will have to file its annual accounts in like manner as does a public company. Briefly the principal requirements necessary for the "exempt" variety are that there must not be more than fifty debenture holders, that another company must not be a shareholder, debenture holder, or director, that neither the company nor its directors are party to an arrangement whereby the policy of the company is directed by persons other than directors, members, and debenture holders or their trustees, and that there must be no nominee holdings. There are certain exceptions to this latter provision, as where a trust corporation holds shares or debentures as executor or trustee or where the shares are in the name of a bank or finance house or nominee thereof as security for accommodation. (See Section 129 and the 7th Schedule to the Companies Act, 1948.) A private company must now supply each of its members and debenture holders with a copy of its accounts not less than 21 days before the date of the annual general meeting.

Fraudulent Conveyance. Particular care must be exercised when the conversion of a customer's business into a limited company is followed by a request for accommodation, for, if a trader transfers his assets and liabilities to a limited company without the consent of each and every one of his creditors, the transaction may be interpreted as a fraudulent conveyance. A fraudulent conveyance is not necessarily a dishonest transaction, but one that defeats or delays a man's creditors; it does not imply a dishonest motive or a state of insolvency.

Such a conveyance is an act of bankruptcy, and if within

three months of its date a petition and Receiving Order result, the trustee's title will relate back to the time of the conveyance and invalidate the transaction. This will mean that the sale of the assets by the trader to the company can be set aside and such assets will revert to the trustee in bankruptcy, rendering void and valueless any debenture or charge given by the newly constituted company to the bank.

The case of *In re Sims, ex parte A. E Quaife* v. *W. Sims and Lloyds Bank Ltd.* (1930) is an instance illustrating this risk. In this case, a builder and contractor as a preliminary to obtaining additional working capital in the shape of a bank advance, converted his business into a private limited company, which took over his assets and assumed responsibility for his liabilities. Bank accommodation was then arranged against the security of a mortgage debenture on the company's assets.

The vendor of the business omitted, however, to notify his creditors that he had converted his business into a limited company, whose assets had been charged by way of debenture to the bank. The first intimation received by his creditors was a notice in the trade papers, and they forthwith began to press for a settlement of their accounts. Instead of explaining the circumstances and making payments on account, the debtor, out of the company's cash resources, paid in full each creditor who in turn pressed him, with disastrous results to the company's liquid position.

Thereupon a petition in bankruptcy was presented against him in his personal capacity by an unsatisfied creditor, on the grounds that he had made a fraudulent conveyance of his property under Section 1 (1) (*b*) of the Bankruptcy Act, 1914. This was followed by a Receiving Order and adjudication in bankruptcy, and the trustee thereupon claimed that the sale and transfer of the bankrupt's assets to the company were void.

The Court made an order setting aside the sale, and the Judge said, in quoting precedents, "The result of these

authorities appears to me to be that a transfer by a debtor of substantially the whole of his property, whether by way of charge or by way of sale, will be an act of bankruptcy, if the necessary consequences of the transfer will be to defeat or delay his creditors."

Conversion of Company Cheques. I have already made brief reference to the necessity for care when dealing with officials of companies in their private and individual capacity, and it is not out of place to enlarge at this juncture on the matter. You are likely to be involved in loss if you permit a director or other official to deal for his private uses with a cheque payable to his company, and also with a cheque drawn by his company.

The following cases reported in the third volume of *Legal Decisions Affecting Bankers* should be studied in this connection: *A. L. Underwood, Ltd.* v. *Bank of Liverpool and Martins Ltd., Same* v. *Barclays Bank Ltd.*, [1924] 1 K.B. 775, and *Souchette, Ltd.* v. *London County Westminster and Parrs Bank Ltd.* (1920), 36 T.L.R. 195.

You must bear in mind that the issue at stake is usually negligence as collecting banker, the transactions themselves not being forbidden by statute. The negligence lies in not making inquiries as to the circumstances under which the cheque in question is being diverted from the company. You will find this point brought out in the Underwood case.

At times, where a denial of negligence would appear to be of little avail, a frequent defence is that the bank is a holder in due course rather than a collecting agent, and you will recall that negligence is immaterial in such a case, provided, of course, that it does not amount to notice of defect of title. But supposing that you can show that you have by express or implied agreement permitted your customer—the delinquent official—to draw against the cheque before it was cleared—and this, according to the learned Judge in the Underwood case, qualifies you as a holder for value—you are not yet out of the wood, as

the case of *Alexander Stewart and Son, of Dundee, Ltd. (in liquidation)* v. *Westminster Bank Ltd.*, [1926] W.N. 271 showed.

At first sight this case would suggest that in every instance where a director misapplies his company's cheque, after endorsing it on behalf of the company, a banker who seeks to set up as a holder for value will not succeed, because the endorsement will be regarded as unauthorised, and, hence, in accordance with Section 24 of the Bills of Exchange Act, 1882, will be on all fours with a forgery.

The case in question, heard in the Appeal Court, is only briefly reported in *Weekly Notes* and cannot be regarded as establishing the above proposition in all circumstances. You will no doubt recall that to the lay mind, at any rate, it seemed in direct conflict with the decision in *Morison* v. *London County and Westminster Bank Ltd.*, [1914] 3 K.B. 356, where it was laid down that a signature could not be regarded as genuine for one purpose and a forgery for another.

It would appear that even if an endorsement can be regular in one case—where the cheque is properly dealt with—and unauthorised in another—where the cheque is dealt with by a director for his own uses in fraud of the company—a banker might still be able to succeed as a holder for value against the company. For if you look up Section 24 of the Bills of Exchange Act, 1882, you will notice that it qualifies the inoperative effect of an unauthorised signature by saying "unless the party against whom it is sought to retain or enforce payment of the bill is precluded from setting up the forgery or want of authority."

In other words, the doctrine of estoppel can be invoked against the company if you can show that the endorsement of the cheque was within the ostensible authority of the director acting as the company's agent.

In the case of *Lloyd* v. *Grace Smith & Co.*, [1912] A.C.

716, it was held that the principal is liable for the fraud of his agent acting within the scope of his authority whether the forgery is committed for the benefit of the principal or for the benefit of the agent. In the Stewart case there was no ostensible authority upon which the bank could rely, for it never treated Sir John Stewart as an agent of the company.

However, in view of the subtle doctrines involved in these matters, you will doubtless agree that to put matters beyond the possibility of loss the only safe course to pursue is to refuse to allow a director to deal with a cheque, either drawn by or payable to his company, in the absence of a proper authority.

We have dealt so far with cases where the fraudulent customer has been known to be an official of the company which is the payee or drawer of the cheque. Are you bound to refuse to credit the account of a third party with a cheque payable to a company if you are unaware of his fiduciary capacity? The decision in the case of *London and Montrose Shipbuilding and Repairing Co., Ltd.* v. *Barclays Bank Ltd.* (1926), hitherto cited in support of such a practice, was reversed on appeal.

While possibly the appeal case cannot be taken to establish the general principle that it is negligence to credit a company's cheque to any other account without inquiry, yet in view of the evidence tendered by bankers in the case of *Savory* v. *Lloyds Bank Ltd.*, [1932] 2 K.B. 122, to the effect that it is the recognised custom of bankers to query such transactions, it is possibly the wise and expedient course to inquire in every case where a cheque payable to a company is being diverted from that company's account.

It is considered by competent authorities that where evidence of such a general banking practice has been tendered any disregard thereof would certainly be held to be negligence. Bankers possibly have only themselves to thank for this state of affairs, for, as the Editor of the

Journal of the Institute of Bankers remarks in the December, 1931, issue, a cheque is, after all, a negotiable instrument, and the endorsement over of a company's cheque to a third party is certainly not in conflict with statute.

Company Liability on Bills. The directors of a company are both agents and trustees, and provided they make it clear that they are acting as agents they will escape personal liability on any document they execute on behalf of the company. There have been many cases in which holders of negotiable instruments to which a company's name has been put have sought to make the directors personally responsible when the company has been unable to pay the money due on such instruments.

There are three essential conditions for establishing the liability of a company on a bill of exchange. Firstly, it must have capacity to contract in such a way. Secondly, the signature must be in sufficient form to bind the company. Thirdly, the signature must be placed on the bill by someone acting under its authority.

Let us see what these three conditions amount to. As to capacity, you might with profit look up Section 22 of the Bills of Exchange Act, 1882. A trading company has implied power to enter into bill transactions, but non-trading companies must have power specially given to them in their memorandum. In practice, however, you will find that specific powers are given in the memorandum—be the company of a trading or non-trading type—to draw, accept, and endorse bills of exchange.

As to the sufficiency in form of the company's signature, its name must be stated without abbreviation. In *Stacey & Co., Ltd.* v. *Wallis and Others* (1912), 28 T.L.R., 209, the suggestion was made that the word "Limited" abbreviated to the customary "Ltd." would invalidate the signature, but the Court vigorously rejected this suggestion. Apparently "Co. Ltd." can take the place of "Company Limited" without infringing Section 108 of the Companies Act, 1948, which provides that the

company's name shall be mentioned in legible characters on all bills, cheques, etc.

Apart from this, if the full name of the company is not stated on all bills, notes, endorsements, and cheques, a penalty of £50 falls on the responsible parties who signed or authorised the document to be signed, and furthermore, if the instrument is not paid by the company such party will be personally liable on it (Section 108 (4)). Not only must the company's name be stated in full, but the proper formula must also be used as provided in Section 33, which says that the bill must be signed "in the name of, or by, or on behalf, or on account of the company."

There seems no doubt that the mere name of the company would be a sufficient signature according to the above section, but obviously a banker does not accept an endorsement of a cheque, let alone a drawing thereof in such a fashion, as there is nothing to show that it was written by someone in authority. A common form of endorsement to-day is "The A.B.C. Co., Ltd., X.Y., Secretary." Here you have the name of the company—the essential thing—followed by the name and description of the person who wrote or impressed it as an indication that it was done under authority.

This is a good discharge for the paying banker, but it will possibly *not* exempt the *official* who signs from personal liability, for you will recollect that the Bills of Exchange Act, 1882, Section 26 (1), states that the mere addition to a person's signature of words describing him as an agent, or as filling a representative character will not exempt him from liability. Thus officials of companies should be advised to make it plain, when executing negotiable instruments for their principals, that they sign in a representative capacity only, by prefixing "for" or "on behalf of" or "per pro" to their company's name.

And that brings me to the third essential condition to establish a company's liability on a bill—its signature must be written or impressed by someone authorised so

to act. Does this mean that you are bound to confirm that the person signing on behalf of the company was armed with the proper authority? This would be an awkward and cumbersome doctrine in the case of negotiable instruments, and, in fact, has no place in company law. There is a rule of law known as the rule in *Royal British Bank* v. *Turquand*, which protects people in their dealings with limited companies.

Broadly speaking, it amounts to this—if you find a company official doing acts on behalf of his company which the articles permit him to do when duly authorised, you are entitled to assume that authority has in fact been given to him; you are under no duty to ascertain that the authority which the articles say he could use has actually been put into his hands by the board or the company.

Thus the articles of a certain company provided for the drawing of bills by the managing director as and when authorised by the board; the managing director drew bills in fact without such authority and in fraud of the company, and it was held that the company could not repudiate the bills, outside parties being entitled to assume that the erring official was actually clothed with the authority which the articles decreed could be put into his hands (*Dey* v. *Pullinger* (1921), 37 T.L.R. 10).

This rule has been subject to two radical modifications in recent years as illustrated by the two cases, *Kreditbank Cassel* v. *Schenkers, Ltd.*, [1927] 1 K.B. 826 and *Houghton and Co.* v. *Nothard Lowe and Wills*, [1928] A.C. 1. It is now pretty certain that, firstly, you will not get any protection from the rule if the transaction is unusual or abnormal, or not one which you would expect the person engaging the company to be entrusted with. Secondly, you cannot rely on the rule if, in fact, you were not at the time aware of the provision in the articles for the delegation of powers to the party whose signature you are seeking to enforce as binding on the company.

This means that where you are asked to discount a company's acceptance—a company who probably will not be in account with you—which is signed, say, by one director and the secretary, you should, strictly speaking, satisfy yourself from the articles that one director and the secretary are the parties authorised to bind the company on negotiable instruments.

In practice, however, you do not go to such lengths—you possibly rely on the practice of sending the bill to the bank where it is domiciled with a request for confirmation of the acceptance, assuming that if the proper parties have not signed, the company's banker will draw your attention to the irregularity. Frequently, I imagine, you take no such course, preferring to take a fair business risk.

If you are asked to confirm the acceptance of a bill domiciled with you, you should not only look to the genuineness of the signature but also satisfy yourself that the provisions of the articles are being followed.

Bankrupt Directors. One of the disabilities under which an undischarged bankrupt labours is that he must not obtain credit for more than £10 without disclosing his state, and this naturally restricts his trading activities before discharge. There used to be two time-honoured methods of overcoming this trouble—the bankrupt got a solvent party to cloak his business activities—the bankrupt's wife is probably not unknown to you in this guise—or he formed a private limited company—a strictly family affair in which the predominant party and managing director was himself.

This second and easy way out of the difficulty is no longer available, for Section 187 (1) of the Companies Act, 1948, makes it a criminal offence for an undischarged bankrupt to act as a director or to take any direct or indirect part in the management of a company without the leave of the Court by which he was adjudged bankrupt.

An exception is made in the case of undischarged bankrupts who were so acting on 3rd August, 1928, and

have continued to act since that date, and whose bankruptcy was prior to such date.

If it comes to your notice that a director of a company which banks with you is involved in bankruptcy proceedings you should make sure that he does not continue to act on behalf of the company if an adjudication order is made. An act of bankruptcy, a bankruptcy petition, a receiving order, is not sufficient—he is under no disability unless and until the final step of adjudication is taken by the Court.

Disclosure to Board of Trade or Director of Public Prosecutions. You are no doubt aware of the legal duty on a banker's part to observe secrecy about his customer's affairs—a duty based on the confidential relationship existing between banker and customer. This duty is far-reaching and not only covers information gleaned from the customer or his account, but to all knowledge of the customer however obtained. This duty of secrecy is not an absolute one however and there are occasions (see *Tournier* v. *National Provincial Bank, Ltd.*, 1924), where a banker is permitted to disclose confidential matters concerning his customer. One of these cases is where disclosure is under compulsion of law.

Under this heading come the powers given to the Board of Trade in Sections 164-171 of the Companies Act, 1948, to appoint inspectors, where irregularities are suspected, to investigate and report on a company's affairs. A duty is laid on all officers and agents of the company by Section 167 to produce to such inspectors all relevant books and documents. By Section 167 (5) the expression "agents" includes the bankers of a company. Likewise by Section 334 where the Director of Public Prosecutions proposes to institute proceedings following the winding up of a company, he may require the company's banker to give him all assistance in connection with the prosecution.

Borrowing by Companies. Perhaps the most frequent source of trouble arises when dealing with company

customers in the matter of borrowings. As we have seen, a limited company, being the creation of statute, has all its activities regulated by law, and when borrowing proposals are put forward by its directors, due regard must be paid by the bankers to the necessary legal formalities involved.

I advocate the observance of some sort of uniform technique in this matter, and suggest that you must, in the first instance, address yourself to three questions. Has the company power to borrow? If so, what is the method prescribed? And are there any limits of borrowing imposed on the company or its directors?

You should first of all refer to the memorandum of association to ascertain if the borrowing of money is specifically mentioned in Clause 3, which sets out the objects and powers of the company. In the case of a trading company the power to borrow need not be expressly mentioned, for it can be inferred whenever such a power may reasonably be regarded as incidental to a company's business. Now, borrowing being a usual feature of trading activities, the power to borrow may fairly be assumed in the case of a trading company. With a non-trading company there must be something in its memorandum to show, expressly or by implication, that the company may borrow.

Inasmuch as in the case of most companies—trading or non-trading—borrowing powers are expressly mentioned in the memorandum, no difficulties usually arise as to construing borrowing powers. You should, nevertheless, not allow the uniform mention of powers to borrow in the memorandum to lure you from making specific reference to a company's power to borrow in each and every case.

Closely related to power to borrow is power to give security, and here again this is usually set out in great detail in Clause 3 of the memorandum as including power to give mortgages, debentures, debenture stock, bills, scrip, and to charge all or any of the company's property, present and future, including any uncalled capital.

If a company has express or implied power to borrow it has implied power to give security for such borrowing by charging or mortgaging its assets, but even so if there is express power given to charge security, regard must be paid thereto in case any limitations exist.

The next question to settle is the *method* of borrowing. Usually the articles put the exercise of the company's borrowing powers into the directors' hands by a separate clause authorising them to borrow, or by a clause giving them the right to exercise all such powers that could be used by the company itself and are not required by the articles or statute to be exercised by the company in general meeting. This latter is the substance of Article 80 of Table A.

Occasionally you will find that any power of borrowing must be exercised not by the directors but by the company in general meeting, and consequently you should closely scrutinise the articles to see if the exceptional method of borrowing by the company in general meeting is laid down.

Having settled that the company can borrow and give security, and ascertained by whom such borrowing must be undertaken, the question of any limits imposed must be tackled, and here again do not assume that your particular company has adopted the same requirement as, I imagine, the majority of companies has adopted—namely, Table A—but make careful reference to he company's memorandum and articles.

Although it is exceptional to find any limitation put on a company's borrowing powers in the memorandum, it is not unknown. Invariable reference should be made in the first instance to that document, for if any restriction is found therein and your company customer borrows in excess of that restriction, your position is well-nigh hopeless. The borrowing is beyond the powers of the company, and any excess cannot be ratified by the general meeting, neither can you avail yourself of any of the

company's security held to cover such borrowing, nor yet can a remedy be sought in getting the borrowing powers of the company enlarged.

If it happened that the money had been credited to the company's current account by way of loan and had not been spent, a banker might get an injunction restraining the company from spending the money; otherwise the only remedy is to seek to get yourself subrogated to—placed in the shoes of—the creditors who had been paid with the proceeds of the advance.

Having ascertained that there are no limitations in the memorandum, you should next turn to the articles to find what they have to say about the extent of the directors' borrowing powers. If by any chance the borrowing powers of the directors are exceeded, your position is not so critical as where the borrowing powers of the company are exceeded, for you can get the company in general meeting to ratify any such excess, or by special resolution it can enlarge the directors' borrowing powers. Any such ratification puts the borrowing on a regular basis and creates an enforceable debt (*Turner* v. *Union Bank of Australia* (1877), 2 App. Cas. 366).

Table A. Most companies frame the borrowing clauses of their articles on, or adopt the relevant article of, the Table A of the particular Companies Act under which they are incorporated.

In ascertaining any limitations on borrowing in the articles you should proceed as follows—

Firstly, ascertain the date of the company's incorporation. If the company was incorporated between 1862 and 30th September, 1906, and either had no articles or adopted Table B, its borrowing powers are unlimited, for Table A of the 1862 Act contained no limitations. As from 1st October, 1906, Table A was revised, and the powers given thereunder were restricted to the amount of issued capital, unless a general meeting authorised otherwise. (Article 73.)

If the company was formed after 31st March, 1909—when the Companies (Consolidation) Act of 1908 came into force—and filed no articles or adopted Table A, the directors are limited in their borrowings to a sum equal to the amount of issued capital, unless authorised to exceed such amount by the company in general meeting. This is the substance of Article 69 of Table A of the 1929 Act.

A new Table A has been provided for the Companies Act, 1948. Article 79 thereof reproduces Article 69 of the 1929 Act as regards borrowing powers, save that in computing the amount outstanding, temporary loans in the ordinary course of business from the company's bankers can be ignored. Furthermore no lender is concerned to see if the limit is observed.

It may be that the company has its own articles which adopt part of Table A, and in such a case you must find out if the borrowing article is excluded. If not, Table A will apply. In this connection you must bear in mind Section 8 of the 1948 Act, which provides that "in so far as the articles do not exclude or modify the regulations contained in Table A, those regulations shall . . . be the regulations of the company in the same manner and to the same extent as if they were contained in duly registered articles."

A few quotations from various articles may help. "The directors may from time to time at their discretion borrow any sum or sums of money for the purposes of the company, provided that the whole amount so borrowed and outstanding at any one time shall not exceed £10,000." Here you have an example of a definite limit beyond which the directors cannot go.

"There shall be no borrowing on the security of the assets of the company without the consent of the preference shareholders." An unsecured borrowing would appear to be in order without the consent of such shareholders.

"The amount borrowed is not to exceed the amount of the preference share capital." In this case no preference shares had been issued, and accordingly there was no restriction on the company's borrowing until such capital was issued (*In re Johnston Foreign Patents, Ltd.*, [1904] 2 Ch. 234).

"The borrowing powers of the directors shall not at any time exceed two-thirds of the current value of the company's property." This is obviously a most unsatisfactory method of limiting borrowing powers, for such assets of the company might well be of varied type, and it would be difficult to arrive at the meaning of "current value."

However, in all cases where the articles do not speak plainly as to a company's borrowing powers, the banker as a condition of lending can insist on the articles being altered, and this, you will recollect, only requires a special resolution of the company.

If you are dealing with a company with definitely limited borrowing powers, you must make sure that you are not participating in any irregular lending. One method is to lend by way of a loan, and in such a case, having loaned a fixed lump sum that is within the company's powers, you cannot be concerned in any *ultra vires* lending, should the company borrow elsewhere to such an extent as to make its total borrowings in excess of the prescribed figure.

But it is often inexpedient to insist on a borrowing on loan account, and if you consequently lend by way of overdraft it is necessary to get a certificate from the secretary at frequent intervals, certifying to the regularity of the company's total borrowings. In estimating the total borrowings of a company, debentures outstanding, mortgages, private loans and any domestic schemes, such as staff deposit funds, must be taken into consideration.

Here I may indicate the usefulness of scrutinising a company's balance-sheet each year; not only does it

give you a view of the company's liquid position, but it supplies the data for computing the total borrowings by the company, not forgetting that occasionally a mortgage is shown as a deduction from the relative property on the assets side.

Any discounting of bills by a company does not fall into the category of borrowing unless the bills are in the nature of accommodation paper.

Then as regards resolutions—if the borrowing must be exercised by the company, you will require a certified copy of the resolution of the general meeting authorising the borrowing.

If the borrowing may be exercised by the directors, it is usual to call for a certified copy of the resolution of the Board so as to make it plain that the advance is granted at the request of the directors as a body and not merely at the request of those directors who draw cheques on the company's account.

If the directors have borrowing powers as in Table A, 1929, any borrowing in excess of the amount of issued capital having to be sanctioned by the general meeting, it is customary to ask for a certified copy of the resolution of such meeting if you find that the directors are exceeding the powers given to them by the articles. Strictly speaking, I submit that you need not inquire as to this resolution, for the rule in *Royal British Bank* v. *Turquand* (1856), 25 L.J.Q.B. 317, will protect you. That is to say, if you are aware that the articles empower the directors to exceed their borrowing limit when authorised by the general meeting, and you find them doing so, you are entitled to assume that the necessary authority has in fact been given to them. Nevertheless, I think it is the practice of bankers to require a resolution in such a case.

It is sometimes suggested that, where the directors have exceeded their powers, an action may lie against them personally for misrepresentation, or breach of an implied

warranty of authority. But where their powers are deducible from the memorandum and articles of association it is difficult to see how, in the absence of deliberate fraud, a lender could complain of being misled, for the memorandum and articles are public documents for all the world to peruse.

Application of Borrowed Moneys. Assuming that you have established the regularity of a company's proposed borrowing as regards the amount, are you bound to see that the money is applied for the purposes of the company? You will recollect that the memorandum usually contains a power to borrow for *the purpose of the company's business*, and it might at first sight appear that a lender must see that the money is being applied accordingly.

But in *In re David Payne and Co.*, [1904] 2 Ch. 608, it was held that a lender is under no such duty. Of course, if he had any actual knowledge that the money was going to be used for a purpose inconsistent with the company's business or for a purpose forbidden by statute, he could not enforce payment of the debt. As a banker usually requires to know the purpose of an advance, he should make sure that the company is not embarking on a borrowing inconsistent with its powers or with statute.

For example, if the advance is required to enable the company to lend in turn to a director for the purchase of its own shares, it should not be granted, for such a loan on a company's part is forbidden by Section 54 of the Companies Act, 1948. A banker is under no duty to satisfy himself, however, that the borrowing is being applied to the purpose for which it was asked.

Company Borrowing—Security. Assuming that you have now satisfied yourself as to the company's power to borrow, that the amount asked for is within the limits prescribed by the memorandum or articles, and that the purpose of the borrowing is not inconsistent with the company's objects, the next question to which you will address yourself is the security for the advance.

For our purpose we can divide the security into two categories: firstly, the type which does not depend for its validity on any sort of registration; and, secondly, the type which is unenforceable unless registered at Bush House in accordance with the provisions of the Companies Act, 1948.

As examples of the first class of security we will take guarantees and stocks and shares, neither of which presents any difficulties. The joint and several guarantee of the directors of a borrowing company is desirable, whether the directors are charging assets of the company or not. It is, after all, not unreasonable to ask the directors to implement their faith in their company's prospects by making themselves jointly and severally responsible for the company's debts, notwithstanding that other security is taken in addition.

Furthermore, the modern form of guarantee usually has embodied in it a clause something like this: "And further the bank may recover against us . . . notwithstanding that the principal being a limited company may have exceeded its borrowing powers or that the borrowing from the bank may have been *ultra vires*." Thus, in a case where the borrowing turns out to be beyond the powers of the company or the directors, you still endeavour to make the directors personally liable for the debt.

Care is required where directors already engaged under a joint and several guarantee for a company's advance arrange for the issue of a debenture to the bank to cover the same borrowing, for by so doing they get some personal advantage. The case of *Victors Ltd.* (*in liquidation*) v. *Lingard* [1927], 1 Ch. 323, will illustrate the point at issue. The directors of Victors Ltd. guaranteed an advance of £25,000 by a bank, and later passed a resolution that there should be issued to the bank £30,000 first debentures as security for the same debt. The debentures were duly issued, and later Victors Ltd. went into liquidation.

Thereafter an action was brought by the liquidator

claiming a declaration that these debentures were invalid, for the articles of association of the company provided that, while no director should be disqualified from entering into contracts, arrangements or dealings with the company, he should not vote as a director in respect of any such contract, etc. The object of the article was plainly to ensure that the directors should not be put into a position where personal interests conflicted with their duty as officers of the company.

Now the issue of debentures would obviously relieve them to some extent as regards their personal liability as guarantors, for the bank would have recourse under the debenture to the assets of the company. The Court accordingly held that the directors were personally interested in the arrangement made regarding the debenture issue, and consequently the resolution was null and void, and so likewise would have been the debentures issued by virtue of it, except that in this instance the liquidator was prevented from challenging the validity of the debentures on account of the course of events subsequent to their issue.

Hence it is a good plan, where you are taking composite security in the shape of debentures and a guarantee* of the directors, to get the debentures duly issued before the guarantee is signed, and then there can be no attempt to invalidate the debentures on the score that the directors who authorised their issue were benefiting thereby, inasmuch as their personal responsibility for the debt was accordingly diminished. Far better, however, is it to get the resolution authorising the issue of the debenture passed by the company in general meeting, a wise procedure also if it is proposed to charge a company's assets where the directors' guarantees are already held.

Guarantee by Company. Occasionally you find a holding company guaranteeing a subsidiary company; in all cases of guarantees by companies you must make sure

* This would apply equally where any other form of personal security had been lodged by a director.

that a clear power to enter into a contract of suretyship can be construed from the objects clause of the memorandum of the company giving the guarantee. I suggest that, if there is any ambiguity whatever, it is expedient to get competent legal advice, for if the giving of a guarantee is beyond the powers of the company there can be no ratification, and the security is worthless. Frequently Clause 3 of the memorandum will include power to guarantee contracts, which probably covers the guaranteeing of a borrowing, which is a form of simple contract. A company is prohibited from guaranteeing a borrowing by one of its directors, unless it is an exempt private company or the director is its holding company. Section 190.

Charge on Stock Exchange Securities. With regard to any holdings of stocks or shares in the name of a borrowing company, they can be charged by the completion of a memorandum of deposit, which can either be sealed by the company or signed on its behalf by duly authorised officials. As in the case of a guarantee, if the letter of deposit is under hand you should file with it a certified copy of the resolution authorising the parties to complete the document, and the stamp duty will be sixpence only.

If the letter of deposit is sealed (a very unusual method), you should see that the seal is properly witnessed and that the instrument is stamped with an impressed stamp at the rate of five shillings per cent on the highest amount you propose to lend if the document is drawn to secure all moneys, care being taken to cover any excesses over such amount by additional stamping within the necessary thirty days.

In taking a company's holding of stocks and shares as security, care must be taken to see that they are not already the subject of a specific charge in a debenture issue, and it would be as well to ascertain, where any such issue gives a floating charge, that there is no restraint therein on the company's power to give a subsequent

charge to rank side by side with or in front of such floating charge.

If, after the stocks and shares have been charged to you as security, you receive notice that the company has issued a debenture specifically charging its assets, including such stocks and shares, remember you are in the position of a first mortgagee receiving notice of a second mortgage, and accordingly are bound to break the company's account if you wish to preserve your right against your security.

Registration of Charges. We now come to the types of security that require registration at Bush House in order to be effective, and you are probably all aware that Section 95 of the Companies Act, 1948, has enlarged the list of charges that are registrable to nine. I imagine that there are three of these charges that principally interest us as bankers—namely, a charge on land, a charge to secure an issue of debentures, and a floating charge. Registration has to be effected within 21 days of the creation of the charge, not of the date of the advance secured by the charge. In this connection it must be remembered that the date of execution is not necessarily the date the instrument bears, but the date when it was actually signed or sealed.

Although it is the company's duty to effect registration, in practice bankers usually register the charge either directly or through their solicitors. This is permissible by Section 96 of the Companies Act, 1948, which says: "Registration of any such charge may be effected on the application of any person interested therein." The section further empowers the lender to charge the borrowing company with the registration fees. The Registrar will brand the instrument of charge with the registry stamp and issue a certificate of registration, which should be filed with the security unless the company insists on its possession.

Unless the charge is registered within the prescribed period of 21 days, the effect will be serious for the lending

banker, for it will be void against a liquidator or any creditor of the company, and all the remedy the banker will have will be to sue the company forthwith as an unsecured creditor. Furthermore, a subsequent chargee, though having express notice of your prior unregistered charge at the time he takes his security, will prevail over your charge (*In re Monolithic Building Company*, [1915] 1 Ch. 643).

Where registration has not been effected within 21 days, the High Court may grant relief and extend the time for registration if satisfied that the omission was accidental, inadvertent, or not likely to prejudice any creditors. Application to the Court would appear to be the proper course to pursue, and I suggest that to destroy an unregistered mortgage and to start afresh with a new charge, is a doubtful method, unless the advance in question has been paid off. The penalty of £50 a day to which officers of the company are liable if a charge is not duly registered applies to *other persons* who are knowingly parties to the default, and, possibly, includes the lending banker.

Vacation of Charges. The cancellation of a charge is effected by enrolling a memorandum of satisfaction with the Registrar. This must be done by the company on Form 49, which includes a statutory declaration by a director and the secretary as to the truth of the memorandum. The Registrar will advise you, as the owner of the charge, that he has received a memorandum of satisfaction for registration and thus give you an opportunity to object if it is not in accordance with the facts of the case.

Before the coming of the Companies Act, 1948, difficulties arose where a portion of the property charged was sold by a company, as often happened where a building estate was being developed. Naturally the purchaser required the property he had bought removed from the charge enrolled at Bush House and if he was not content for the conveyance to recite the company as vendor and the bank as mortgagee, incorporating a release on the latter's

part, there was nothing for it but to vacate the whole charge and to re-charge the remaining property with all the expense of fresh stamp duties and the trouble of registering the new charge. This was because the Registrar was not empowered to register a memorandum of partial satisfaction where the charge was for all moneys or for all sums not exceeding a named amount or for a fixed sum plus increases.

By Section 100 of the 1948 Act the Registrar is now permitted to enrol a memorandum of partial satisfaction in cases where the debt has been partially satisfied or part only of the property concerned has been released from the charge. This concession will be of considerable benefit to bankers.

Borrowing Against Land. We will now look to the formalities involved when lending to a company on the security of its property by way of mortgage. The first thing to do is to satisfy yourself that no prior encumbrances exist thereon. You should, therefore, have a search made in the Bush House Register to see if any mortgages or debentures giving a charge on the property in question are already enrolled. The Registrar does not issue search certificates in the ordinary way—the search must be a personal one.

There is no need to search the Land Charges Register for prior mortgages, for by Section 10 (6) of the Land Charges Act, 1925, a land charge to secure money, given by a company, is sufficiently protected by registration at Bush House under Section 95 of the Companies Act, 1948, whether the charge is backed up by the relative deeds or not, and if it is registered on the Land Charges Register it is registered in the wrong place.

It must be remembered, however, that there are certain encumbrances, such as pending actions, writs, winding-up orders, restrictive covenants, and equitable easements, that will not be revealed by a search at Bush House—their home is on the Land Charges Register. I suggest,

therefore, that searches in some cases should be made in the Land Charges Register to see if any of the many matters capable of registration in the five registers affect the company. Particularly if you are dealing with a land development company, or if you are lending money to a company for the purpose of erecting property on a vacant site, these additional searches should be made.

Of course, if you are dealing with land having a registered title as evidenced by a land certificate, you should search the Land Register of Titles for any such matters. Furthermore, there are other registers which in certain cases require to be searched—the local registers kept by borough, urban or rural councils and by county councils—in order to see if your security is likely to be affected by any town planning schemes. Likewise the deeds registries of Yorkshire require searching where land in this county is concerned.

Assuming that you are satisfied that the property offered as security is unencumbered, you will get your mortgage form executed under seal unless you are prepared to take an equitable charge signed under the hand of duly authorised officials. Registration at Bush House should follow within 21 days, and stamping within 30 days of execution.

If you are dealing with land situated in Yorkshire do not forget that registration of a legal mortgage at Bush House will not excuse registration on the appropriate deeds register of the particular Riding.

If you are dealing with a land certificate of the company, in addition to registering your charge at Bush House you must register it at the Land Registry or give notice of deposit of the land certificate.

What is the position if, after you have taken a charge over the company's property, a debenture or a second charge is registered at Bush House, and you do not receive direct notice from the second chargee? Does such registration constitute notice to all the world, including

you? There is no decided case on this point, but there are certain dicta, in *Wilson* v. *Kelland*, [1910] 2 Ch. 306, that such registration constitutes constructive notice. Consequently a diligent search of *Perry's Gazette* or similar periodical should be made, so that if notice of such a registration is seen the necessary steps can be taken to crystallise the position by breaking the current or loan account.

Registration of Oral Charge. You are all familiar with the obstinate type of director who is prepared to lodge the deeds of his company's property to secure the company's advance, but will not sign any document of charge. You are no doubt aware that an equitable mortgage can be created by the mere deposit of documents of title with intent to charge; now in the case of a company a charge is invalid unless registered, but can you register an oral charge, a charge not evidenced by any written instrument?

The answer is "Yes," and if you will refer to Section 95 of the Companies Act, 1948, you will notice that it requires particulars of the charge to be delivered to the Registrar, together with the instrument, *if any*, by which the charge is created. This suggests the possibility of a charge by deposit without any memorandum, and, in practice the Registrar will enrol such a charge if the banker gives particulars, such as the amount, the parties thereto, and the date, which will be the date of the deposit of the deeds.

Again, there is another and familiar type of obstinate director who will not charge the company's deeds on account of a profound aversion to mention in *Perry's Gazette*, thinking, possibly, that it has the odium attaching to mention in the *Police Gazette*. Unlike the former party, he is quite ready to sign any charge, provided that you do not register it. It is useless taking such a security, for non-registration invalidates the charge. A compromise is sometimes reached by getting a written undertaking from

the company not to dispose of or charge the deeds deposited with you without your consent. But, remember, this is in no sense a charge, and you have no effective security available against the company's liquidator or creditors. It is undesirable to get an undertaking from the company to give a charge if called upon, for such an undertaking would require registration.

Land Held by Nominee. Caution is needed when accepting, as security for a company's advance, deeds ostensibly in the ownership of a director, for it is not uncommon for a company's property to be held by a director or directors as nominee. If such is the case, it is the company's property that is being mortgaged, and consequently any charge should be given by the company and registered accordingly.

I suggest that if there is any evidence that the directors hold the property in a trust capacity, that it is part of the company's assets, you would be unable to enforce your security in the event of disaster overtaking the company, for the liquidator would not let you regard it as collateral security lodged by the directors, and would require it to be brought into the company's assets. In such a case you could not hold the security against him, for it is neither charged by the company nor registered against it.

Of course, if at the time you took your mortgage from the ostensible owner of the property you had no notice, express or constructive, that it was held in a fiduciary capacity, and you acted honestly and without gross negligence, you would be able to hold your security against the company. I imagine that one of the surest methods by which you would have notice of the company's interest in the property would be where it was separately included among its assets on the balance sheet in your possession.

It is the practice in some quarters where deeds are lodged by directors in their beneficial ownership to get a statutory declaration from them to the effect that they do not hold in any sort of nominee or trust capacity

whatever. This is an earnest that you have taken all reasonable precautions.

Industrial and Provident and Friendly Societies. You will occasionally conduct accounts with societies of a provident or industrial type, which are registered with limited liability, not under the various Companies Acts, but under the Industrial and Provident Societies Act, 1893, or the Friendly Societies Acts. Any charge given by such a body over its property is not registrable with the Registrar of Companies, and as no provisions are made in the above Acts for enrolment of charges, your security cannot be perfected by registration, except in so far as it falls within the Land Charges and Land Registration Acts.

Debentures. The other two types of security for consideration that require registration on the Companies Register are a charge given to secure an issue of debentures and a floating charge. In practice you will find that a floating charge is usually incorporated in a debenture, and hence is not registered separately.

None of the Companies Acts has attemped any definition of a debenture, but for our purpose it may be called an acknowledgment of indebtedness. In *Palmer's Company Precedents*, Vol. 3, certain characteristics of a debenture are given which may help us to grasp the essential notion of the document.

Firstly, it is generally one of a series, but in the case of a banking security a single debenture is usually issued; secondly, it is generally issued by incorporated companies, although occasionally you do find an issue of debentures by an unincorporated body, such as a club or committee; thirdly, it is generally under seal, although it can be issued under hand; fourthly, it generally provides for repayment, except in the case of irredeemable debentures; fifthly, provision is usually made for the payment of interest; and, lastly, the document usually confers a charge, although this is not an essential part of the instrument.

Where a company issues debentures to a bank as security for an advance, the document is either specially drafted by the bank's solicitor, the contents being based on a common form adapted to meet a particular case, or a standard printed form is used. Occasionally a banker may take part of a series of debentures from the borrowing company, but usually a single debenture is given.

Provisions in Debenture to Bank. You will find that the following matters are generally provided for in the usual type of debenture issued to a bank. Reference will be made to the resolution of the company or directors, as the case may be, authorising the issue of the debenture, thus making it plain that it is a valid document. It will sometimes be drawn in favour of the bank, and in other cases in favour of a nominee company, although, of course, it could be drawn in blank, and thus be payable to bearer. It may be drawn for a specific lump sum, or drawn to secure all advances made or to be made.

The advantage of a debenture for a fixed sum over an "all money" debenture is that the bank will be able to sell the debenture should it so desire, while in the latter case a sale will not be easy. When a debenture for a fixed sum is taken it is usual for it to be deposited under a separate memorandum of deposit given under the seal of the company or under the hand of duly authorised officials.

This further document is necessary in order that the debenture, being issued for a lump sum, shall be available in respect of a fluctuating advance by way of overdraft or loan. It also has the merit of linking up the debenture with the company's banking account, as otherwise the bank might find its powers limited to the ordinary rights of a debenture holder and be unable to sue the company on the overdraft, as apart from the debenture.

The memorandum provides that the debenture shall be held by the bank as security for all moneys owing now

or in the future, including interest, commission, stamp duties, and all costs and charges incidental to the creation of the debenture and its realisation. It sometimes provides that, on a sale of the debenture, the condition as to "all moneys" shall cease to operate and the purchaser will then possess a debenture for the fixed amount named therein.

It will also provide for interest at the banker's usual fluctuating rate, notwithstanding that a fixed rate may be mentioned in the debenture itself. The memorandum also gives the bank an express power of sale over the debenture.

Returning to the main document, you will usually find that it is expressed to be payable on demand, that interest is stipulated for at a fixed rate, or at a fluctuating rate with a minimum, to be payable with quarterly or half-yearly rests. Then the company charges as security all its undertaking and property present and future, including its uncalled capital, and there follows a list of conditions of the issue of the debenture, providing, among other things, that the debenture shall be a first charge on the undertaking and property of the company and shall constitute a fixed charge on specific property, generally listed in a schedule, and also on any fixed machinery, plant, goodwill, and uncalled capital.

You must remember that such a fixed charge is usually of an equitable nature and gives you none of the rights and remedies of a legal mortgagee other than the power to appoint a receiver. In some instances the company gives a legal mortgage over its real property by using the statutory formula of "a charge by way of legal mortgage," which you will remember is a short way of giving a long lease in the case of freeholds and a sub-lease in the case of leaseholds. Whatever sort of charge is given, however, the company should always covenant to deposit the relative title deeds with the bank.

In addition, the debenture will generally constitute a

floating charge on all the other assets of the company, which covenants not to create any further mortgages or charges to rank side by side with or in front of the debenture in question.

It must not be forgotten, however, that if a subsequent lender takes as security a fixed charge on assets covered by your floating charge, he will get priority notwithstanding that he has notice of your floating charge, provided that he is not aware of this covenant on the company's part. While search at Bush House will reveal your charge, it will not necessarily give details of the contents thereof, and one way to try to ensure that your floating charge will not be sterilised by the creation of a subsequent fixed charge would be by insisting on the company making the issue of your debenture by a special resolution giving full details. A special resolution, of course, has to be filed at Bush House, and hence its contents would be available to all subsequent lenders.

There then follow, in great detail, the conditions under which the moneys secured by the debenture shall become payable. They include a demand in writing on the part of the holder, the default of the company with its interest for, say, two months, the institution of voluntary or compulsory winding-up proceedings, the cessation of business by the company, the appointment of a receiver and the alteration or attempted alteration of its memorandum or articles of association in a manner prejudicial to the bank's security.

Powers are taken, as soon as the principal money owing becomes payable, to appoint a receiver, who is to be deemed the agent of the company. This saddles the company, and not the bank, with responsibility for his acts, defaults, and remuneration. Sometimes the right to inspect the company's books is given—a useful clause in cases where the banker, having a floating charge, wishes to satisfy himself as to what floating assets are at any time subject thereto.

Fixed and Floating Charges. Let us now look at the essential differences between a fixed and a floating charge. A fixed charge definitely hypothecates the company's property concerned; the directors have no powers to dispose of it without the banker's consent, it is mortgaged to the bank. A floating charge is a method of giving a lender some sort of security over a company's assets—more especially its liquid assets—without in any way fettering the company's business activities by requiring the chargee's assent to any dealings with such assets.

Ordinarily such an item as stock could only be charged by way of a bill of sale; book debts could only be charged by way of assignment, and in both cases no dealings could take place without the consent of the lender.

But with a floating charge, both stock and book debts can be charged without in any way hampering the company in its trading activities; it can sell its stock, get in its book debts and use the proceeds as it pleases, while it is a going concern, without consulting the lender.

So paramount is this freedom of a company to use at its will any assets subject to a floating charge, that the sale by a company of its whole undertaking and business to a new company was held to be valid, notwithstanding that its assets were the subject of a floating charge, as such a sale was authorised by the company's memorandum of association (*Foster* v. *Borax Co.*, [1901] 1 Ch. 326).

A floating charge is converted into a fixed charge when anything happens to crystallise the position of the company *vis-à-vis* the lender; in other words, when any of the conditions just outlined in the debenture come to pass—for the most part when the company defaults in making repayment and a receiver is appointed, or when it goes into liquidation. Then the charge ceases to float, it fastens on the assets concerned, and the lender has a specific charge on such assets with all the remedies of possession or sale. But you must take some positive

step in order to crystallise the position—merely making demand on the company and awaiting developments is not sufficient.

There is possibly no need for me to point out the undesirability of taking a debenture containing only a floating charge as security, for the company is at perfect liberty to sell its stock, call in its book debts, pay off its unsecured creditors, and leave you high and dry with a charge that has nothing to fix on when the time arrives to deal with your security. Likewise, it is unsound banking to make an advance on an unsecured basis to a company with a debenture issue, for the holders of such debentures will have a prior right to be satisfied out of the assets covered by the debentures, and there will possibly be nothing left for the unsecured creditors, of whom you will be one.

Occasionally where a company without a debenture issue has been borrowing on an unsecured basis, you think the time has come to put matters on a secured basis in view of the unsatisfactory trend of your customer's affairs. There being no fixed assets left uncharged and no point in taking the guarantee of the impecunious directors, you may, as a desperate remedy, take a floating charge on the company's assets in view of the stock that it is carrying. Your hopes of security may be illusory, for should the company go into liquidation within twelve months of the date of the charge, it will not avail you except for any fresh moneys lent on the strength of the charge, unless it can be shown that the company was solvent immediately after the creation of the charge (Section 322, Companies Act, 1948).

In other words, the company, with insolvency in sight, will not be allowed to prefer you to other creditors by giving you security for an existing debt. Of course, if you take a debenture with a *specific* charge, in such circumstances it may possibly amount to a fraudulent preference.

Then, suppose you take a floating charge to secure an existing debt and the company goes into liquidation within twelve months, what is the position if the account is still overdrawn but has been active since the date of the floating charge in the sense that there have been payments into and payments out of the account? It would appear that the third rule as to the appropriation of payments, known as the rule in *Clayton's* case, could be applied, and credits to the account since the date of the charge appropriated to the debt existing at the time the charge was taken, subsequent drawings being in the nature of fresh accommodation.

Thus the balance due at the time the company goes into liquidation can be said to be "cash paid to the company . . . subsequently to the creation of and in consideration for the charge" (Section 322, Companies Act, 1948). The case of *In re Thomas Mortimer, Ltd.* (1925), bears out this contention.

Formalities in Taking Debentures as Security. Now let us glance at the formalities to be observed in taking debentures as security. It is essential, of course, to make sure that no mortgages or debentures are outstanding that are likely to affect your security, and this means searching the company's file at Bush House. But you must also make sure that there are no uncancelled redeemed debentures in existence.

A company may redeem or pay off a debenture, but need not cancel it; it can keep the debenture on its register of charges and put it into cold storage, as it were, usually by placing it in the name of a director as its nominee. Such a debenture can be re-issued, and the Act of 1929 altered the conditions surrounding the keeping alive of such redeemed debentures and also the conditions attaching to their re-issue.

Before 1929, in order to keep a redeemed debenture alive, the company had to do something to shew such an intention, such as transferring it to a nominee for the time

being. Any such debentures that were reissued, started life afresh—they were subject to any charges that might have been given subsequent to their first issue.

By the Act of 1929, re-enacted in Section 90 of the 1948 Act, a redeemed debenture is not cancelled unless the company by resolution or some other act indicates that it is cancelled, or unless there is any express or implied provision in the articles. Furthermore, by Section 75 of the 1929 Act as re-enacted by Section 90 of the 1948 Act, uncancelled debentures re-issued after 1st November, 1929, go forth into the world with all the priorities attaching to them that they had at the time of their original issue. It is not difficult to see, therefore, that any mortgage or debenture that you may take might possibly be postponed to an old debenture re-issued after you had taken your security. The risk, though remote, is real, and therefore inquiries should be made of the company concerning any such debentures, and if they are in existence the directors should be asked to cancel them.

Having satisfied yourself that the charge given in the debenture is not subject to prior encumbrances, you will proceed to get your debenture duly sealed by the company and to get registration effected at Bush House within 21 days of its execution. A copy of the certificate of registration will be endorsed on the debenture. A debenture giving a charge on land will not require registration also as "a charge on land or any interest therein." (Section 95 (7), Companies Act, 1948.)

If the debenture contains a specific charge on registered land or land in Yorkshire, registration will be required at the respective registries, also. The debenture will want stamping within thirty days of its date at the rate of five shillings per cent on the amount covered, or if it is drawn to secure all moneys, on the highest amount it is proposed to lend for the time being.

Appointment of Receiver. It may be that to safeguard your advance it is necessary to appoint a receiver to lay

hands on the assets charged under your debenture, in order that they shall not be dissipated by the company. You will probably take powers in the debenture to put a receiver in, but whether you act under such power or apply to the Court for the appointment, the Registrar must be informed within seven days on Form 53, otherwise a penalty of £5 per day is incurred.

Usually the power of appointment of a receiver contained in a debenture is accompanied by power for such a party to take possession of the company's assets and to carry on and manage the business, and to use the net profits of the company and the proceeds of sale of the security in paying the expenses of the receivership, interest on the debenture, and the principal sum due.

If a receiver is appointed at the instance of an outside party the first thing to do is to see the evidence of his appointment in the shape of the copy of the Order of the Court or the document under the hand of the debenture holder(s). If you have a credit balance on the company's account you must pay it over to the receiver, provided that a floating charge was contained in the debenture, otherwise the receiver's powers will only extend to the assets that are the subject of the fixed charge.

If, in addition to the credit balance, you have claims on the company in the shape of a debit balance on another account, what is your answer to any attempt on the receiver's part to lay hands on the credit balance? Inasmuch as a banker always has a right of set-off between two current accounts in the same right when anything happens to crystallise the position, it would appear that you would be entitled to set such credit balance off against any debit accounts of the company, and only to pay over to the receiver any resultant balance.

Nevertheless, in cases where companies borrow against credit balances or require net accommodation on two or more accounts some banks insist on a resolution of

the directors admitting a right of set-off in order to put the matter beyond all doubt.

Liability of Receiver. If a receiver for debenture holders opens an account with you, an application by him for an advance requires especial care. You must discriminate between a receiver appointed by the Court and a receiver appointed under powers given in the debenture or trust deed.

In the first case he is an officer of the Court and is the agent of neither the company nor of the debenture holders. Usually he will apply to the Court for leave to borrow any moneys required, and, if successful, an Order is generally made giving the bank a charge over the assets of the company, in priority to the debenture holders' claims, in respect of any advances made. Care must be taken to see that any limits imposed by the Court are observed. In the absence of the leave of the Court to borrow, the receiver will be personally liable.

In the case of a receiver appointed out of Court he will be considered the agent of the company or the debenture holders, according to the terms of the debenture or trust deed. Where he is not expressly constituted the agent of the company, he will be looked upon as the agent of the debenture holders, who will be liable for any debts properly incurred by him.

If power is given in the document appointing the receiver for him to carry on the business of the company, there is possibly an implied power for him to mortgage its assets to that end, but it is advisable to get the debenture holders to postpone their claims on the company's assets in favour of the charge given by the receiver.

A case heard in the Court of Appeal was concerned with the question of liability of a receiver for a borrowing undertaken in performance of his duties. In *Mudd* v. *National Provincial Bank Ltd.* (1931), the facts were that the receiver for the debenture holders of a brick company had opened an account with the National Provincial

Bank Ltd., and in an effort to preserve the business of the company had overdrawn the account without security to the extent of £2818. Apparently to regularise matters, he put into writing the following admission: "I beg to inform you that I accept full liability for the amount owing to the bank by me from time to time in respect of my account with you as receiver of the above company."

When sued for the money he contended that this letter was not an admission of personal liability, but only of liability as receiver. In confirming the finding of the lower Court that the liability was a personal one, the Master of the Rolls said: "It seems to be that the liability is accepted by Mr. Mudd in the plainest and simplest words."

This sort of position cannot arise since the passing of the Companies Act, 1948, for Section 369 makes a receiver appointed out of Court personally liable for any contract entered into in performance of his functions in like manner as a receiver appointed by the Court.

Likewise a receiver appointed out of Court is now entitled under Section 369 to apply to the Court for directions—a facility not previously available to him.

Wages Cheques. A source of considerable trouble when you are dealing with a borrowing company which appears to be hovering on the brink of liquidation, is the payment of its weekly wages cheque. The non-payment of such a cheque may well precipitate the crisis which all parties have been trying to avert; the payment thereof may only result in increasing a bad debt. There is now, however, some measure of relief found in Section 319 (4) of the Companies Act, 1948. This provides that a lender of money to a company for the payment of salaries or wages shall have the same right of priority in a winding-up as the clerk, servant, workman or labourer etc., would have had if he had not been paid. In a winding-up such a party is entitled to payment in full of salary or wages for the

preceding four months up to a sum not exceeding £200. Consequently, any advance by a bank for the express purpose of providing wages or salaries can be regarded as a preferential claim up to the statutory limits in the event of the company's liquidation. Some banks accordingly charge wages cheques to a separate account in circumstances where the company's fortunes are not too bright and proof as a preferential creditor in the event of liquidation would be of advantage.

The case of *National Provincial Bank* v. *Freedman and Rubens*, reported in the *Journal* for October, 1934, is justification for adopting the above course.

CHAPTER IV

GUARANTEES

I PROPOSE to direct your attention to some aspects of the guarantee as a type of banking security and to survey these aspects in some measure of fullness from a practical point of view. I want first of all, however, to stress the necessity for a working knowledge of the forms of charge in use by your respective offices, and in doing so I am only emphasising what a distinguished line of legal gentlemen have said on this platform when discussing the legal implications of banking securities.

I am pleading this matter for two reasons. Firstly, although intending borrowers are prone to put pen to paper when signing a form of charge, without pausing to inquire as to its significance, you are occasionally confronted by an enquiring customer or an inquisitive guarantor, who wants to know the why and the wherefore of certain clauses in the document before him, and in such a case it is highly desirable that you should be able to enlighten him in a general way.

Indeed, I suggest that in view of the far-reaching powers that are put into a banker's hands in the average security form, it is expedient, if not essential, to point out to a prospective guarantor that by signing your form of guarantee he is contracting out of most of the rights and remedies with which the law has endowed a surety; to explain to a borrower against title deeds that in signing a bank form of mortgage, he contracts out of many of the rights appertaining to a mortgagor. Of course, in some cases it is expedient to suggest to such a party that reference should be made to his solicitor.

Secondly, a working acquaintance with these forms is desirable, so that in cases of emergency you should know

what latent powers are wrapped up in them, in order to be able to take up a prompt line of action in the interests of the bank.

The Guarantee. We will now consider the guarantee as a type of banking security.

There is an illusory comfort about a guarantee, probably due to the fact that it is fairly easy to obtain, for when you have rehearsed with your customer most of the orthodox forms of security you find that his house is already mortgaged, his War Loan—that faint far echo of his war-time profits—has been sold, he has already borrowed on his life policy from the insurance company, and when you desperately fall back on the suggestion of a guarantee, the borrower can usually suggest a relative or a friend who can be persuaded to stand as surety for his advance.

Be very careful, however, to let the persuasion come from your customer and not from yourself, for if the prospective surety commits himself to a guarantee you will find yourself in an awkward plight if, when you have to request him to fulfil the terms of his undertaking, he alleges that he entered into the contract at your behest. "A contract of suretyship is one in which I think that everything like pressure used by the intending creditor will have a very serious effect on the validity of the contract" (Fry, J., in *Davies* v. *London and Provincial Marine Insurance Co.* (1877), 8 Ch.D. 469).

The security behind a guarantee is the instant ability of the guarantor to pay when called upon, and although a banker's unqualified report on a surety's financial standing may give an advance a well-covered aspect, it must be remembered that men's fortunes may change in a night, and the experience of the last few years is that an undoubted guarantor is often hit by the very circumstances that cause the debtor's default; or possibly his investments have so shrunk in value, or his resources are so bound up in the equities of mortgaged properties,

that he must needs crave your indulgence and ask for time.

In other words, you must never forget that an advance against a guarantee unsupported by collateral security is in effect an unsecured advance to the guarantor, and you should accordingly take every means of ascertaining that the guarantor's financial strength is such as will permit of a ready discharge of his liability, not only now, but also at a future date. If he happens to be a customer of yours, this should not be difficult, but should he bank elsewhere, it is necessary to appreciate the subtle distinctions in a banker's opinion—"is good for the sum named" is on a different plane from "should be good for the sum named," for example. In these days of changing fortunes it is especially necessary that status enquiries about guarantors should be answered with particular discrimination and care, and if the surety's resources are not liquid due emphasis should be laid on this feature.

Enquiry of Banker. It is the practice in some quarters to enquire of the surety's banker for a sum in excess of the amount of the guarantee, as a sort of insurance, and I think that in such a case you should, in due course, inform your brother banker of the actual amount of the guarantee that is taken, otherwise he will have an inflated idea of his customer's commitments. It is a sound practice to enquire concerning a joint and several guarantor as if he were in fact a sole guarantor, for you may have to rely on him alone.

One further drawback about a guarantee is that there is usually a sense of grievance on the guarantor's part if he is called upon to pay—that is the last thing he contemplated; he looked upon the obligation as a mere formality, and if he chances to be a customer of yours the enforcement of the liability often strains relations.

Preliminary Formalities. Now let us look at the formalities attendant upon the giving of a guarantee. Firstly, do not make any advances on the oral promise of a

prospective surety to give a guarantee, for by the Statute of Frauds any promise to answer for the debt of another must be in writing and signed by the surety, or there must be some signed memorandum or note of the agreement. If you made an advance before a guarantee was signed, relying on the word of the intending guarantor, you would have no remedy against him if he eventually refused to commit himself in writing. Then, do not be content with an informal document in letter form if you can possibly avoid it, but get the surety to execute your standard printed form, which, as we shall see later, provides for all contingencies and is drawn to give the maximum of safeguards to the bank. Experience shows that the enforcement of an informal guarantee is often a costly and litigious matter.

Again, it sometimes happens that a guarantor, acting under legal advice, objects to some of the clauses in your standard form; be careful to get competent guidance regarding any addition or deletions, for the printed form of guarantee is the product of expert legal minds; every sentence has a definite significance, and the deletion or addition of a word or two may rob you of some remedy if and when you have to enforce payment.

A case in point is *Westminster Bank Ltd.* v. *Sassoon*, where the guarantor desired to limit her liability to a period of twelve months. A clause was, therefore, added to the document to the effect that "this guarantee will expire on 30th June, 1925." On this date the account was broken, the borrower defaulted and recourse was had to the guarantor, who claimed, however, that her liability had vanished in smoke at the expiration of twelve months. Of course, the intention was obvious, that at the end of the period the position should crystallise, and "expire" was the wrong word to use—"determine" is the word to be employed in such a case.

Occasionally, as a matter of convenience, you may get the form of guarantee executed before you have made the

necessary enquiries concerning the worth of the guarantor. In such a case be careful to make it plain to the borrower and the surety that the signing of the guarantee has not committed you to the advance.

If you happen to take a guarantee limited to a certain period, in addition to breaking the account at the date the guarantee is determined, it is advisable to remind the guarantor that he is liable for the figure standing in your books, otherwise he may mistakenly think that your silence implies that his liability is finished. This is a matter of expediency however, and the absence of advice on your part would not release the guarantor. Likewise, the debtor should be reminded in due course that the crucial time is approaching when a cessation of credit facilities on the strength of the guarantee will occur.

Then see that the guarantee is executed in your presence or in the presence of another banker or of a solicitor, who can duly witness the signature of the guarantor. To entrust the document to the debtor for completion is to invite trouble later on, for the guarantor may set up misrepresentation as to the document he signed, or possibly may contend that his signature has been forged. In *Carlisle and Cumberland Banking Co.* v. *Bragg*, [1911] 1 K.B. 489, the execution of the guarantee was left to the debtor, who induced the guarantor to sign under the pretext that the form was an insurance paper. The bank was not allowed to recover on the guarantee, on the ground that the guarantor's mind did not go with his pen.

Offering Advice to the Guarantor. While an astounding number of people are content to put their signature to a guarantee form without pausing to enquire as to the nature of the liability undertaken, you occasionally find an inquisitive man who desires to know exactly what it all means, and in such a case the knowledge of your form of guarantee, which I urged just now, will be useful. In fact, I suggest that whether the guarantor is prepared docilely to append his signature without enquiry or not, it is

expedient to enlighten him as to the liability he is undertaking. Happily, this does not involve a tortuous explanation of each and every clause in the document, for if you warn him that once he has signed the guarantee he has bound himself irrevocably to the extent of the sum named therein, and that there are no circumstances in which he will be able to wriggle out of his liability, you have acted in perfect fairness. He should be told that if he pays he cannot expect to inherit all your rights and remedies against the debtor unless his payment satisfies the whole debt. In some cases a copy of the guarantee is given to the surety, who duly acknowledges it on the original document.

Incidentally, it is not a bad idea to point out to the debtor, who sees in the guarantee an end of all his troubles, that if the bank gets paid by the guarantor the slate is not wiped clean as far as he (the debtor) is concerned, for the right of recovery is only shifted from the banker to the guarantor, who now becomes the borrower's creditor.

Women as Guarantors. This matter of explaining the purport of a guarantee, whilst merely expedient in the case of the male surety, becomes imperative in the case of a woman guarantor. Notwithstanding the enlargement of woman's status economically and politically during the last half century, the presumption of law is that she is incapable of understanding a business transaction by the exercise of her own wit—when it is to her advantage not to understand. Thus, it is the practice of bankers, wherever possible, to arrange for a guarantee by a woman to be executed under the guidance of her solicitor, in order that she may not afterwards avoid her liability by asserting that she did not understand the implications of the document she executed. If a married woman guarantees her husband's account it is usual to have on record not only competent evidence that she knew what she was doing, but also an admission that she entered into

the contract freely and voluntarily and was not subject to the duress of her husband.

There is a tendency in some quarters to think that this precaution is particularly necessary in the case of a married woman, because she is presumed to be under the dominion of her husband, and the case of *Bank of Montreal* v. *Stuart and Another*, [1911] A.C. 120, is usually cited in support of this contention. But this dealt with special circumstances, where a wife who was a confirmed invalid was prevailed upon to give a guarantee for her husband, and despite her denial of duress or misrepresentation it was held that she was not a free contracting party, "her evidence merely showing how deep rooted and how lasting the influence of her husband was." I submit that the decision in this case does not vary the earlier case of *Howes* v. *Bishop and wife*, [1909] 2 K.B. 390, where in seeking to avoid liability on a promissory note which she jointly signed with her husband, Mrs. Bishop pleaded, amongst other things, that she was subjected to the undue influence and pressure of her husband.

It was held that the relation of husband and wife is not similar to that of solicitor and client, guardian and ward, trustee and beneficiary, where undue influence can be presumed. The heading of the Law Report says: "There is no general rule of universal application that the rule of equity as to confidential relationship necessarily applies to the relation of husband and wife so as to throw on the husband, or the person who is suing the wife, the onus of disproving an allegation of undue influence." One of the Lords of Appeal said, however, "I must not be understood to be laying down a rule that in no case where a wife acts on her husband's instructions and under his influence is it necessary to show that she has received independent advice. There may be circumstances where the mere signing of the document by the married woman is not of itself sufficient to render her

liable on it, but in my opinion there cannot be a general rule of universal application that the rules of the Courts of Equity as to confidential relationship necessarily apply to the relation of husband and wife." Thus, failure to get the admission of a married woman that she guarantees her husband freely and voluntarily would not in itself invalidate the contract, but it is a banking practice to get such an admission as a matter of expediency to shut out any possibility of undue influence being set up by the wife when she is called upon to pay. If you are going to insist on legal advice being tendered in such circumstances, it is just as well that the branch solicitor should not act in case it is alleged later that he was interested on your behalf.

In cases where it is not practicable to get a guarantee executed under the guidance of a solicitor, it is customary to obtain the woman guarantor's signature to a declaration written on the form itself to the effect that the document was explained to her and that she understood its tenor and signed it of her own free will and accord.

Companies' Guarantees. Guarantees given by limited companies should be the subject of special care, for unless there can be construed from the company's Memorandum of Association a clear power to engage in such contracts, the company will not be bound. Unless this power is laid down in the plainest possible terms it is desirable to seek legal opinion on the matter.

Subject to anything in the Articles the guarantee of a company can be executed under the hand of a duly authorised official, and you should file with the document a certified copy of the resolution of the board authorising the official to sign the document. This method involves a sixpenny stamp only, whilst if the guarantee is sealed by the company, *ad valorem* duty at the rate of five shillings per cent on the amount of the guarantee is required.

A certified copy of the resolution of the Board authorising the giving of the guarantee should be taken, in

which it should be stated that the guarantee is to be given in the form and terms of the specimen guarantee attached. Otherwise, if the resolution merely speaks of the giving of a guarantee for £x, trouble may arise subsequently if the company (or, more probably, the liquidator) is called upon to pay, for, as we shall see later, the bank form of guarantee is something very much more than an engagement for a definite amount of money, and it might be contended that the guarantee executed by or on behalf of the company was a very different contract from that authorised by the Board.

In the ordinary way a company is prohibited by Section 190 of the Companies Act, 1948, from *guaranteeing* a director's borrowing (see p. 59).

Whilst on the subject of companies, I may remind you of the possible risk involved in taking the company's security subsequent to the guarantee of the directors, for, if these directors voted on the resolution authorising the charging of the security, and the articles do not expressly permit them to vote on a contract in which they are personally interested, the security may be void as against a liquidator, inasmuch as the resolution authorising its issue was passed by directors who were personally interested, in that their guarantee liability might as a consequence be lightened (*Victors, Ltd.* v. *Lingard*, [1927] 1 Ch. 323). If there are not sufficient uninterested directors to pass the necessary resolution, it should be passed by the company in general meeting.

Guarantees given by a firm should be executed by all partners therein, unless specific authority is given for one to sign on behalf of the others. The power of one partner to bind his co-partners does not ordinarily extend to the giving of guarantees.

A guarantee should not be taken from a minor, for he cannot be bound under the instrument, being incapable of entering into contracts other than for necessaries. The attainment of his majority will not cure the defect,

for a contract of guarantee is not included in the class of contracts which, unless he repudiates them, are binding when a minor reaches the age of twenty-one.

The Banker's Duty to Disclose. It now remains for us to discuss the duty, or otherwise, of a banker to put the proposed guarantor in possession of all material facts concerning the principal debtor. A guarantee does not fall into that class of transaction known as contracts of the utmost good faith, where non-disclosure by one of the parties of all material facts will render the contract void. "The contract between the surety and the creditor is one in which there is no universal obligation to make disclosure" (*Davies* v. *London and Provincial Marine Insurance Co.*, (*supra*)). A banker is not bound to volunteer information concerning his customer—the guarantor must look after himself, and he is not entitled to assume that the banker is going to enlighten him as to the debtor's banking habits or business standing. But suppose that the guarantor asks for information? According to Sir John Paget, you can answer without risk any questions put by the guarantor concerning your relations with the debtor, for the latter's introduction of the guarantor can be looked upon as an implied authority to disclose material information, or the occasion may be regarded as justifying disclosure. (*Vide Law of Banking*, 4th edition, p. 423.) In his note to the *Tournier* case (*Legal Decisions*, Vol. 3, p. 312) Sir John, commenting on the Judge's third instance where disclosure of a customer's account is justified—where the interests of the bank require it—again suggests that relevant questions by a proposing guarantor may be safely answered, as the interests of the bank clearly require that it shall not jeopardise its own security.

I cannot find any case-law on this matter, and possibly a customer would have a hard job if he sued a bank for breach of duty in disclosing the state of his account to a prospective guarantor. Nevertheless, I suggest that

if a guarantor showed a desire to cross-examine you on your customer's banking and business habits, you should endeavour to get the latter's authority for a full disclosure, or try to arrange for a joint meeting with guarantor and debtor.

But if a guarantee is not a contract of the utmost good faith, it is in some instances a first cousin to it. For example, where it is obvious that the guarantor is labouring under a misapprehension regarding the debtor's affairs, the banker must put him right. In a Scottish case (*Royal Bank of Scotland* v. *Greenshields*, [1914] S.C. 259) it was said: "The only circumstances in which a duty to disclose would emerge and a failure to disclose would be fatal to the bank's case would be where a customer put a question or made an observation in the hearing of the bank agent, which would inevitably lead anyone to the conclusion that the intending guarantor was labouring under a misapprehension as to the customer's indebtedness." In other words, to keep your mouth shut in some circumstances is as injudicious and risky as an over-optimistic verbosity concerning your customer; silence in some circumstances is as dangerous as the spoken word. As was said in the case just quoted: "Very little said that ought not to have been said and very little not said which ought to have been said would be sufficient to prevent the contract being valid."

If any information is divulged to the guarantor either voluntarily or otherwise, care must be taken that it corresponds with the facts for "a contract of guarantee, like any other contract, was liable to be avoided if induced by material misrepresentation of an existing fact, even if made innocently." (Lord Atkin in *McKenzie* v. *Royal Bank of Canada*, [1934] A.C. 468.)

While the guarantee is current the banker is under no duty to advise the guarantor of any change in the debtor's position. In *National Provincial Bank of England, Ltd.* v. *Glanusk*, [1913] 3 K.B. 335, where the debtor was

using the guarantee for purposes not contemplated by the surety, it was held that there was no duty on the part of the bank to advise the guarantor.

The guarantor is not entitled to be shown the debtor's account while the guarantee is running, but he can demand at any time to know the extent of his liability. In the usual case where the surety guarantees the whole debt with a limitation on his liability, it has been suggested that he is entitled to know the total figure of the debtor's advance, but I imagine the usual practice is to confine the information to the amount for which the guarantor is actually liable at the time of enquiry.

The Guarantor's Responsibilities. Now let us look at the responsibilities and liabilities which a guarantor undertakes when he binds himself under a bank form of guarantee.

Some of you may wonder why it is necessary to envelop a plain promise to be collaterally answerable for the debt of another in such a welter of words and phrases as is found in the average printed form. It is true that a simple undertaking in writing such as "I guarantee A. B. for a sum of £100" would give you some sort of right against the guarantor, but you would be cramped in your lending relations with A. B. and might easily find yourself deprived of your remedies against the surety. And that is why you find your guarantee form bristling with provisions against certain contingencies—provisions that subordinate the guarantor's rights to those of the bank.

The key to the complicated document in use is found in a right appreciation of the guarantor's position. This arises from the fact that there must be three parties in respect of a contract of guarantee—the principal debtor (the borrower), the principal creditor (the banker), and the surety. The guarantor is a potential debtor of the bank, for he has to pay if the debtor defaults. He is likewise a potential creditor of the borrower, in that if he pays what is due to you he steps into your shoes and is entitled to

all the rights and remedies which you would have over against the debtor. Hence, if there is no principal debtor capable of being sued there is no guarantee as such, for if the surety pays you there is no remedy left for him to pursue. Thus, advances to impersonal bodies like clubs, unincorporated societies, etc., cannot, strictly speaking, be effectively guaranteed, for there is no one capable of being sued for the debt. Likewise, there cannot strictly be a guarantee of an infant's debt, for the guarantor will not have any right of action against the infant, if he discharges his liability. In *Coutts & Co* v. *Browne-Lecky*, [1946] 2 All E.R. 207, two joint guarantors had guaranteed a minor's account, all parties being aware of his infancy. The guarantors successfully resisted a claim by Coutts & Co. for the amount of their liability on the footing that if there is no legal redress against the principal debtor, there is likewise no redress against the guarantor. One bank, at least, provides for this contingency by a clause which recites: "I agree that any sum or sums of money which may not be recoverable from the undersigned on the footing of a guarantee, whether by reason of any legal limitation, disability or incapacity on or of the principal, shall nevertheless be recoverable from the undersigned as sole or principal debtor."

The Guarantor's Rights. Because of the dual position which a guarantor occupies, the law has clothed him with all sorts of rights. "A surety is undoubtedly and not unjustly the object of some favour, both at law and in equity. It is an equity which enters into our system of law that a man who makes himself liable for another person's debt is not to be prejudiced by any dealings, without his consent, between the secured creditor and the principal debtor" (Earl of Selborne, L.C. *In re Sherry* (1884), 25 Ch.D. 692).

I have said that in the absence of other provision, if the surety pays what is due under his guarantee he steps into the creditor's shoes and inherits all the latter's powers

and remedies. Not only is he entitled to an assignment of the guaranteed debt so that he may proceed against the debtor, but he is entitled to the benefit of any of the debtor's securities that are in the creditor's hands to secure the same debt.*

If during the currency of the guarantee the debtor is allowed to deal with any of his securities covering the same debt, the guarantor can claim to be released from his obligation, for this is a case where he is prejudiced by a dealing between the creditor and the principal debtor, inasmuch as the securities which he would be entitled to take if he paid what was due are no longer available.

If the creditor "gives time" to the debtor—to use a legal phrase—that is to say enters into a binding contract to extend credit to the borrower, or takes his note of hand payable at a future time, the guarantor could normally claim to be released, for he has been prejudiced in that, if he paid what was due under his guarantee, he could forthwith turn round on the debtor for reimbursement. But his remedy has been postponed, as the creditor has bound himself not to press for repayment for a definite period.

Once again, suppose your customer, the debtor, is heading fast towards bankruptcy and the bank in common with other creditors agrees to a composition to save the expense of bankruptcy proceedings, the guarantor could repudiate his liability—he has been prejudiced, for, if he chooses to pay up, he will find himself fettered in his rights against the debtor. He might have chosen to find his remedy in putting the debtor into bankruptcy, but this course is now denied him, as the banker has assented to a composition outside bankruptcy.

You will therefore appreciate that a guarantee would be a very embarrassing form of banking security if a surety were left in possession of all his legal rights, and accordingly the modern form of bank guarantee is specially

* See page 108.

drafted to give a banker the utmost freedom of action and to take away from the guarantor all those rights and remedies that would be likely to conflict with the bank's interests.

The case of *Perry* v. *National Provincial Bank Ltd.*, [1910] 1 Ch. 464, is interesting in this connection, as it shows that a surety *can* contract out of the rights with which the law has endowed him. In this case, the bank released the principal debtors under an arrangement whereby it received as consideration for so doing certain debentures of a company formed to take over the debtors' assets. A surety, who had mortgaged deeds as part security for the principal debtors, thereupon claimed his release on the score that the principal debtor having been forgiven, his suretyship was at an end. The mortgage, however, gave the bank power "to compound with—accept compositions from and make any arrangement with the debtors." In the Appeal Court, the surety was held to be still liable, and the Master of the Rolls said: "It is perfectly possible for a surety to contract with a creditor in the suretyship instrument that notwithstanding any composition release or arrangement, the surety shall remain liable although the principal does not."

The Contents of the Guarantee. Let us now address ourselves to the chief stipulations and conditions usually found in a bank form of guarantee. First of all, the precise liability of the surety is laid down; secondly, precautions are taken to prevent the operation of the rule in *Clayton's* case; thirdly, the circumstances under which the bank and the surety can respectively determine the guarantee are enumerated, and, lastly as mentioned just now, the ordinary rights of a guarantor are categorically renounced in favour of the bank.

Firstly, as to the sum involved. It is customary for the surety to guarantee the whole debt, with a limitation on the sum recoverable, rather than to guarantee a specific figure. To the layman this may seem like splitting hairs,

but there is a world of difference between "In consideration of your advancing the sum of One hundred pounds to A, I guarantee the due repayment thereof," and "I guarantee the due repayment of all moneys now or at any time due to you or remaining unpaid by A, provided always that the amount for which I shall be liable shall not exceed One hundred pounds." In the first case the limitation is in the wrong place, and if you were to advance more than £100 the guarantor might be able to avoid payment on the grounds that the contract had been broken—the limitation should never refer to the advance, but to the liability, and the consideration should never be recited as the lending of a definite sum, but in some such form as opening an account with the debtor or continuing his existing account or granting accommodation to him. This is illustrated in *Burton* v. *Gray* (1873), L.R. 8 Ch. 932, where a guarantee was given to a bank as follows: "In consideration of your lending F. B. £1000 for seven days from this date, I deposit certain title deeds." The bank did not strictly fulfil the condition by placing £1000 to the credit of F. B., but allowed him, during the next seven days, to overdraw his account to an amount somewhat less than £1000. It was held that the bank had no lien on the title deeds, as it had not fulfilled the condition.

But more important is the effect of the second formula if the debtor becomes bankrupt. Where the guarantor makes himself responsible for the entire debt, even though he limits his liability, he cannot claim to prove in bankruptcy unless he pays the entire debt, and it is usual for this to be emphasised by a subsequent clause whereby the guarantor undertakes to keep out of the picture and not to prove in competition with the banker on the debtor's estate. If the surety had guaranteed a named sum he could, on payment of that amount, prove for dividend on the debtor's estate, and you would have to reduce your proof accordingly. If, however, he had guaranteed the entire debt with a limit on the amount recoverable, you

are entitled, on payment by him of the sum named as the limit, to place it in suspense and to prove for the entire debt, bringing the guarantor's contribution into account afterwards. A simple case will illustrate the point at issue. If you had a debt of £1000 secured by a guarantee for £500, and your customer failed, you would have to credit the account with the £500 paid by the guarantor and prove for the uncovered balance of the debt—£500. Assuming ten shillings in the pound was paid, you would get £250 from the estate, and thus would make a bad debt of £250. If, however, the guarantee was for the whole debt with a limitation of liability of £500, you could put the surety's payment of this sum on one side and prove for the whole debt of £1000. A dividend of ten shillings in the pound would yield you £500, and this, with the guarantor's payment, would leave you covered for the whole debt. Things do not work out in such a simple manner in practice, but the principle embodied in the example is present in all cases where the whole debt is guaranteed.

The case of *In re Sass, ex parte National Provincial Bank of England Ltd.*, [1896] 2 Q.B. 12, concerned exactly similar circumstances, where there was a guarantee of the whole debt with a limitation of liability and a following clause to the effect that the bank was at liberty to prove for dividends on the debtor's estate without prejudice to its right of recovery from the surety of any balance thereafter owing within the named limit in the guarantee. The trustee in bankruptcy disputed the bank's right to prove for the full debt as it had received from the guarantor the amount for which he was liable. The Court held however, that the surety having paid part only of the debt, had no right to stand in the bank's shoes in respect of the amount he had paid.

The guaranteed debt is usually expressed to include any liability of your customer alone or jointly, including interest, commission and legal costs. Under some forms,

interest and commission charges are recoverable over and above the limit of the guarantee for a period of six months before demand is made on the guarantor. Out of abundance of caution it is the fashion to express the guaranteed debt, not as due or owing by the principal debtor, but as the amount remaining unpaid by him. This precision of phrasing is designed to avoid any attempt at repudiation of liability by the surety on the grounds that on the bankruptcy of the debtor the money is not due or owing by him.

One bank expresses the debt as due or owing by the debtor, but covers itself by inserting later, "Every sum of money which may now be due or owing to you, by the principal, shall be deemed to continue due and owing to you notwithstanding the bankruptcy of the principal." Likewise, the same precaution is taken to cover the decease of the debtor, as it might then be argued that the money is not due or owing by him, but by his estate.

The rule in *Clayton's* case is avoided by relating the liability to moneys now or hereafter owing and by expressing the guarantee as a continuing security. If the guarantee related to an existing debt only, any payments into the account would go towards its cancellation.

The exact significance of the phrase "continuing security" is not always appreciated. Some people think that if a guarantee is given for a limited period it is not a continuing security. Now the effect of these words is to save the operation of the rule in *Clayton's* case—it extends the guarantee beyond the original advance to subsequent advances, and it matters not that the account goes into credit during its currency.

The opposite type is a specific guarantee—one given for a named sum, in which case the advance should be taken on loan account on which all reductions must be permanent, for if a fluctuating overdraft is taken all payments to credit will be appropriated in reduction of the original guaranteed debt. A guarantee may be limited as to time

and still be a continuing security, notwithstanding that during its currency the account fluctuates, for example, between debit and credit.

Determination of Guarantee. Now as to the arrangements for determining the guarantee. On the banker's part the terms of the guarantee usually entitle him to payment on demand or two or three days after demand, once the principal debtor has defaulted. The guarantor cannot expect the banker to pursue every remedy against the borrower before calling on him, and there is no obligation on the banker to resort to the debtor's security before calling on the surety. "It is his (the guarantor's) business to see whether the principal pays and not that of the creditor." (Lord Eldon in *Wright* v. *Simpson* (1802), 6 Ves. 714.)

If it happens that the debtor has resources and is leaving the guarantor in the lurch, a bank will usually take proceedings against him at the guarantor's request, provided that its costs are assured, and in practice, if you hold securities of the debtor, you usually recoup yourself from this source before exerting pressure on the guarantor.

The modern form of guarantee expressly states that payment is guaranteed "on demand being made in writing." Unless demand is stipulated as a precedent condition of payment, the guarantee will require renewing at intervals, for the Limitation Act, 1939, begins to run in such a case in respect of each advance made on the strength of the guarantee—that is, from the time each cheque is honoured.

This would mean in practice that shortly before the expiry of the sixth year of a guarantee under hand you would have to get an acknowledgment (which by the Statute of Frauds must be in writing) of the continuance of the liability on the part of the surety. The efficacy of inserting the words "on demand" in the guarantee is found in the fact that until demand is made on the surety

the Limitation Act does not operate and you are under no necessity to renew the security at intervals.

In such a case there is small risk of the Act operating to your detriment, for even after allowing for the indulgence which a banker is always ready to show to a guarantor, it is difficult to imagine a case where, demand having been made, the banker has let matters slide for a period of six years.

If a guaranteed account has been in credit for a considerable period, and borrowing is then resumed, it is expedient to remind the surety of the existence of his liability, in case he had in mind the guaranteeing of the debtor's account for a special purpose which is now accomplished.

Again, it may be that a guarantee was given for the purpose of financing the debtor in a specific matter, and if and when you are aware that this matter has been accomplished, it is only equitable to see if the guarantor wishes his liability to continue, although from the strictly legal point of view you would be quite safe in continuing advances, notwithstanding that the primary purpose for which the guarantee was given has been accomplished.

It is usual to provide that, in addition to the amount named as a limit in the guarantee, the surety will be liable for interest at five per cent per annum from the date of the debtor's default to the time of payment by the guarantor.

So much for the banker's right to determine the guaranteed liability; what of the guarantor's right to do so? In the absence of any provision to the contrary, he is entitled to give notice to crystallise the position at any time. Usually, however, you will find that the bank stipulates for three months' written notice before the guarantor can determine his liability.

Authorities are at variance as to the banker's right to continue to make advances on the strength of the guarantee during the three months. One school of thought advocates reliance on the literal significance of the words in the notice clause, thus allowing you to continue the

account unbroken until the three months' notice has expired. This may appear inequitable because at the time of receipt of the notice the debt may be inconsiderable, while by the time the notice has expired it may have mounted to a peak figure.

So the other school of thought urges a course of conduct something like this: On receipt of notice, call your customer in and inform him accordingly, arrange to pay cheques already drawn and outstanding, and undertake to honour cheques to be drawn in respect of commitments already entered into, but tell him that, apart from these transactions, no further accommodation will be granted. There is no decided case on this particular point, but fortunately in practice matters can sometimes be adjusted on a basis satisfactory to all concerned.

I imagine that most managers in receipt of three months' notice to determine a guarantee, would take an early opportunity of conferring with both the surety and the debtor and coming to some mutually satisfactory arrangement. It may be that the debtor is a person undeserving of consideration, the sudden withholding of credit from whom would not greatly prejudice his position, while the guarantor is a party whom you would like to placate. In such a case you could demand payment forthwith from the debtor and, on his default, exercise your right to demand payment from the guarantor, thus giving him the opportunity he is seeking of ending his liability.

In this connection, a comment by the Editor of the *Journal of the Institute of Bankers*, on page 151 of Vol. XLIII, is to the point—

"The practical moral to be drawn is that while a bank should not attempt to hold the guarantor to his bargain under conditions which would entail unnecessary hardship to the latter, the clause (that is, for three months' notice) is a useful one which should not be omitted from the banker's form, and which there is good reason to believe the Courts would uphold if the banker, to protect his

own interests or those of his customer, should be induced to rely upon it."

Then you will find that the guarantor gives the banker the express right to make any arrangements he likes with the debtor, to deliver up securities to him relating to the same debt, to grant time to him, to compound with him or enter into any sort of composition, and he renounces his rights to take over any of the debtor's securities until the whole debt, and not merely the guaranteed part of it, is discharged.

Other Stipulations. Finally, there are various stipulations of a minor nature, which experience has shown it is expedient to include. Thus, you will usually find a clause to the effect that the guarantee is additional to and not in substitution of any others given by the guarantor for the same account.

Then the surety covenants not to take security from the debtor in respect of his liability while the guarantee is current without the bank's consent, and further agrees that, if he does do so, the amount of his liability will be increased by the amount by which the dividend received by the bank from the debtor's estate is decreased.

This clause is plainly designed to ensure that the banker's claim against the debtor's estate is not whittled down by the fact that the debtor has earmarked some of his assets for the guarantor's benefit. This covenant is probably so frequently broken because the guarantor is quite unaware of its existence.

It is also usually provided that in the event of legal proceedings being taken to enforce the guarantee, a copy of the debtor's account, certified under the hand of an officer of the bank, shall be conclusive evidence of the state of indebtedness. Occasionally, where a surety has referred the demand for payment to his solicitor, an attempt is made by the latter to get a copy of the borrower's account. You are under no obligation to give this, however, unless and until the matter goes into Court.

A clause, common to most forms, provides for the continuance of the guarantee despite any changes in the parties concerned. Thus, if the principal debtor is a partnership, the constitution of which changes as a result of the death, retirement, etc., of a partner or of the incoming of a new partner, the guarantee given in respect of the old firm will likewise apply to the new firm which has been virtually created by any such changes.

Likewise, the guarantor agrees that his liability shall continue notwithstanding either any change in the name of the bank or the amalgamation of the bank with another concern. Otherwise, if a guaranteed debt was continued after the amalgamation, the guarantor might claim that the amount owing at the time of the amalgamation (for which he would ordinarily be liable) had been wiped out by subsequent payments in, leaving him free.

In a further clause, which is probably of more practical use, the guarantor admits his liability notwithstanding that the debtor, being a limited company or other statutory body, has exceeded its borrowing powers, or has indulged in *ultra vires* borrowings. It is a source of great relief when, finding that a borrowing company has exceeded the powers laid down in its memorandum, or has in some other way engaged in a borrowing beyond its powers, you recall that you have the directors' joint and several guarantee included in your security, containing such a clause. But while it will no doubt avail should a regular borrowing become irregular or if you make an irregular borrowing innocently, I am bound to say that such a clause would be of little avail if you deliberately, with your eyes open, allowed a company to engage in a frankly *ultra vires* borrowing, because you were getting a guarantee for an avowedly illegal purpose.

Let us now see how the foregoing matters work out in practice.

I need hardly remind you that once a guarantee has been determined, whether by notice on the part of the

banker or guarantor, or following bankruptcy of the debtor or the death or bankruptcy of the guarantor, you must break the account; otherwise, by the operation of the rule in *Clayton's* case, any payments to credit will go in reduction of the guaranteed debt and any payments out of the account will not be covered by the guarantee.

In some forms of guarantee there is a clause as follows—

> "In the event of this Guarantee being determined either by notice by me or my legal personal representatives, or by demand in writing by the Bank it shall be lawful for the Bank to continue the account with the Principal, notwithstanding such determination, and the liability of myself or my estate for the amount due from the Principal at the date when the Guarantee is so determined shall remain, notwithstanding any subsequent payment into or out of the account by or on behalf of the Principal."

This is plainly designed to cover the case where, through inadvertence or other cause, a guaranteed account is continued without a break on the happening of determination by one or other of the parties. In the ordinary way, such oversight would result in the rule in *Clayton's* case operating to the bank's detriment as mentioned above. This clause, however, is a cautionary measure which will avoid such an unfortunate course of events. Some people think that it is ineffectual but, in fact, it is otherwise. The rule in *Clayton's* case is not a rule of law but a rule of evidence—the breaking of the account demonstrates the intention of the bank to fix the guarantor's liability at the time.

Any doubts as to whether such a clause has any value were dispelled by the case of *Westminster Bank Limited* v. *Cond*, [1940] where no break was made in a guaranteed account after the guarantee was determined. One of the grounds on which the guarantor sought to evade liability was that the guaranteed indebtedness had been wiped out by transactions on the account subsequent to the

date of determination. The Bank relied on the above clause which was contained in the guarantee and it was held that its effect was to prevent the rule in *Clayton's* case operating in the guarantor's favour.

Where the banker calls on the surety for payment, or the latter's notice to determine his liability has expired, you occasionally open another account for your customer on the understanding that it is kept in credit. Now, when payment is actually made by the guarantor, you are under no duty to bring such credit balance into account—the surety is liable for the debt outstanding at the time the account was broken consequent on the determination of the guarantee.

This was laid down in the appeal case of *In re Sherry, London and County Banking Co.* v. *Terry* (1884), 25 Ch.D. 692, where the Court held that the bank in opening a fresh account on the determination of a guarantee was quite in order in carrying subsequent payments-in to the credit of the new account.

But it must not be forgotten that during the currency of a guarantee a banker cannot arbitrarily divert credits to another account with a view to segregating the liability of the surety, who guarantees the "ultimate balance." This phrase means the balance arrived at by taking all accounts open at the date of determination into consideration, so that before you can state the sum due under the guarantee you must combine all accounts standing in the debtor's name in his own right.

Sometimes, of course, you take a guarantee on the explicit understanding that it is to be applicable to one particular account only, and in such a case the question of the ultimate balance will not arise.

Payments by Guarantor. A distinction must be noted between payments made by a guarantor before the bankruptcy of the debtor and those made subsequent thereto.

In the first case, your action will primarily depend on the intention of the surety who makes the payment. If

he intends it to be a support to his guarantee, and not a discharge thereof, you should place the money on a separate account—usually a deposit account, suitably earmarked. In the subsequent event of the debtor's bankruptcy, you can prove for the entire debt, regarding the guarantor's contributions as third party security, to be used after you have got all you can from the debtor's estate.

If, however, the guarantor intends the payment to be in discharge of his liability you should, in the absence of any provision to the contrary, place it direct to the credit of the guaranteed account and cancel the guarantee. If this payment does not wipe out the debt, you will be at a disadvantage in the event of the subsequent bankruptcy of your customer, for you can prove only for the balance of debt remaining.

This was made plain in the Scottish case of *Mackinnon's Trustees* v. *Bank of Scotland*, [1915] S.C. 411, where the sum paid by the guarantor before the debtor's bankruptcy was placed to a suspense account, although it was intended by the guarantor as a discharge of his guarantee. It was held that the bank was bound to deduct such money from the balance due before proving in the subsequent bankruptcy of its customer.

Among other things it was held that the action of setting off interest on the guarantor's contribution against interest on the principal debt showed that the bank regarded the money deposited as part payment of the principal debt.

But some banks use a form of guarantee whereby the surety not only guarantees the whole debt, with a limitation on the sum recoverable from him, but also covenants to stand aside and not to compete with the bank as regards recovery from the principal debtor whilst any part of the latter's liability to the bank is unsatisfied. Here is a specimen clause—

This guarantee shall be applicable to the ultimate

> balance that may become due to the bank from the principal, and until repayment of such balance in full, the bank shall be entitled to retain, realise or otherwise dispose of in such manner as the bank shall think fit any securities now or hereafter held by the bank and without any liability to account to any of us for any proportion of such securities or the proceeds thereof until the said ultimate balance shall have been satisfied, *and in the meantime none of us shall take any steps to enforce any right or claim against the principal in respect of any sum or sums paid by us or any of us to the bank hereunder.*

Now, the effect of this appears to me to be as follows: The guarantor not only contracts to pay a named sum in respect of his guarantee of the whole debt, but also he contracts to keep out of the way, to leave you with undiminished rights against the debtor's estate, while any part of the guaranteed debt—the entire debt—is unpaid.

A guarantor may pay up to-day, leaving you with a balance unsecured, and bankruptcy may not descend on your customer until a year or more afterwards, but, provided you have not done anything when accepting his money to suggest that you have waived the other part of the contract, you are free to prove for the entire sum due from your customer, ignoring the surety's contribution.

This will mean that the guarantor cannot prove in respect of the sum paid under the guarantee, for there cannot be a double proof in respect of the same debt. Of course, you should be careful not to cancel the guarantee or hand it back to the guarantor when he pays, for this will clearly be an implied waiver on your part of all the covenants made by the surety in the instrument. You should, of course, break the guaranteed account, place the guarantor's contribution to a suspense account, and open a new account in the debtor's name if you are going to continue banking relations with him.

This may appear an arbitrary proceeding, especially as the time during which the guarantor must, like his money, be kept in suspense is indefinite, but it gives point to my

suggestion that an intending surety should have it made plain to him at the outset that he can hope for none of the ordinary rights of the surety to be vouchsafed to him while any part of your customer's debt remains unsatisfied.

In putting this matter before you I have not overlooked a passage in the judgment in the *Mackinnon* case—"in other words, the payments made before sequestration (that is, bankruptcy) go to reduce the debt for which the creditor may rank, whatever may have been the terms of the guarantee under which the payments were made." Firstly, this is a Scottish decision, which might not necessarily be followed in an English Court, and, secondly, it is not certain whether the words are part of the judgment, or merely *obiter dicta.* If a sum is paid into the debtor's account, plainly emanating from the guarantor, it is desirable to ascertain if it is paid into the account in the ordinary course of business or in part discharge of his liability.

Fraudulent Preference. Another clause found in some bank forms of guarantee reads as follows—

> "No assurance, security or payment which may be avoided under any enactments relating to bankruptcy or under Section 265 or 266 of the Companies Act, 1929, or any statutory modification thereto and no release settlement or discharge which may have been given or made on the faith of any such assurance, security or payment shall prejudice or affect your right to recover from the undersigned to the full extent of this guarantee."

This may seem somewhat cryptic, but its insertion is due to the fact that banks have during the past few years been unwittingly exposing themselves to loss owing to their guaranteed customers having been guilty of fraudulent preference.

This state of affairs arises in this wise: Section 44 of the Bankruptcy Act of 1914 as amended by the Companies Act, 1947, enacts: "Every payment made by any per-

son . . . with a view of giving a creditor or any surety or guarantor for the debt due to such creditor, a preference over the other creditors shall, if the person paying is adjudged bankrupt on a Bankruptcy Petition presented within six months after the date of paying be deemed fraudulent and void as against the Trustee in Bankruptcy."

Section 320 of the Companies Act, 1948, applies the above Section of the Bankruptcy Act to companies. Now there have been several cases where insolvent debtors, seeing bankruptcy ahead, have paid off their guaranteed overdrafts to the detriment of their other creditors, with the express intent of benefiting their guarantors. The debt having been satisfied, the bank, in ignorance of the circumstances, has cancelled the guarantee, only to find that subsequently the debtor's trustee or liquidator has successfully set up fraudulent preference against the debtor. The result has been that the bank and not the guarantor has had to refund the sums concerned to the debtor's trustee and, having cancelled the guarantee, has had no recourse against the guarantor. The cases of *Re Lyons* (1934) and *Re Conley* (1937) were decided against the banks concerned on this score and so likewise was the more recent case of *In re M. Kushler Ltd.* (1943).

Hence the merit of the above quoted clause which is designed to preserve a bank's right against the guarantor in such a case. It is just as well for a banker to retain the form of guarantee where the surety has been released by repayment of the advance by the debtor and circumstances do not rule out the possibility of fraudulent preference.

Sections 92 (4) and 115 (4) of the Companies Act, 1947*, give some relief to bankers in cases where fraudulent preference of a guarantor or surety is alleged, by empowering the Court to grant relief and to give leave to bring in the guarantor as a third party in the action.

* These sections cover bankruptcy; winding up is similarly provided for in Sect. 321(3) of the Companies Act, 1948.

Now, as to payments made by the guarantor subsequent to the bankruptcy of the principal debtor. You will recollect that the right of the creditor to place such moneys in suspense and to prove for the whole debt, where the whole debt is guaranteed with a limitation on the amount recoverable, was expressly recognised in the case of *In re Sass*, [1896] 2 Q.B. 12, and emphasis is usually laid on this in the form of guarantee.

In the course of the judgment in *In re Sass*, already mentioned, it was said: "If the surety is a surety for part of the debt, and the surety has paid that part, then by virtue of that payment, the right of proof of the principal creditor becomes the right of proof of the surety. In my judgment, the surety became a surety for the whole of the debt. It is true his liability was limited, and he, having paid only a part of that debt, has, in my judgment, no right of proof in preference or priority to the bank."

Consequently, on the bankruptcy of your customer, you proceed to advise the Official Receiver of the amount due to you from your insolvent customer, making no mention of the guarantee, and in due time you will prove for the total debt, less the value of any security held, and the proceeds of any realised security, belonging to the debtor, but without regard to any sums since paid by the guarantor. After you have received everything possible from the debtor's estate by way of dividend or sale of his security, you fall back on the guarantor's contribution, returning any surplus to him.

If it is a case of the bankruptcy of the guarantor, the account of the debtor should be stopped in order to establish the amount for which you can prove against the surety's estate. The Official Receiver should be forthwith advised of the contingent liability and, later, should be given, in the form of proof, the figure which is claimed from the surety's estate, assuming that your demand on the debtor for repayment or alternative security is fruitless.

Although a guarantor guarantees the whole indebtedness of your customer with a limit on his liability, this does not necessarily entitle you on the guarantor's bankruptcy to prove for the entire indebtedness of your customer. The position is crystallised and you can only prove for the amount named as a limit in the guarantee, or the amount of the debt, whichever is less.

Where an account is secured partly by a guarantee and partly by the debtor's own security, and the guarantor pays up to the extent of the limit engaged for, he is entitled to a proportionate part of the debtor's security if the guarantee covers part only of the debt. But if, as is customary, it is drawn to cover all advances, with a limit, he is not entitled to any part of the debtor's security until the whole debt is satisfied.

This is generally made plain by a clause: "The bank shall be entitled to retain, realise, or otherwise dispose of any securities now or hereafter held, without any liability to account to me for any proportion of such securities until the said ultimate balance shall have been satisfied." Occasionally, however, a guarantor, aware of the security position, will volunteer to discharge the whole debt and not merely the sum mentioned as the limit of his liability. In such a case you must put him in your shoes and hand over any securities you hold of the debtor's.

This will mean giving the surety the same rights as you possess over the security, by transferring, for example, a mortgage you hold. It may be that you have a debt covered partly by security lodged by the debtor, partly by a guarantee, and partly by security lodged by a third party. If the guarantor chooses to pay the entire debt, he must be given all the security held—that of the third party as well as that of the debtor—and it matters not that he was unaware of the other collateral security.

If it happens that a guarantor discharges his liability and this clears the debt, which has also been covered by security lodged by the debtor, no subsequent advance

should be made to your customer on the strength of such security, unless you have given the guarantor opportunity to exercise his right to have the security assigned to him.

Death of Guarantor. The death of a guarantor will not determine the guarantee before notice of such happening reaches the bank. When notice is received your action will depend on the terms of the guarantee. Ordinarily the account should be stopped, notwithstanding that the document contains the clause stipulating for three months' notice of termination by the guarantor.

In some forms, however, you will find a clause whereby the guarantor binds his personal representatives as follows: "In the event of my death the liability of my legal personal representatives, and of my estate, shall continue until the expiration of three calendar months' notice in writing of the intention of my executors or administrators to determine the guarantee."

If in such a case the surety's executors give you notice of his death, it will not operate to determine the guarantee. There must be a definite notice of revocation. You should, of course, take the earliest opportunity, on notice of the death of the guarantor, of advising his personal representatives not only of the existence of the liability but of the terms under which it can be determined.

In some quarters it has been suggested that such a clause should not be relied on, but in *Coulthart* v. *Clementson* (1879), 5 Q.B.D. 42, it was said, "If, indeed, the contracting parties desire that on the death of the guarantor a special notice to determine the guarantee shall be necessary they can so provide in the guarantee itself, and such a provision will, of course, bind the estate."

But in some circumstances it might be not only inequitable but even dangerous for you to make further advances, even though the executor had not given notice to determine the guarantee. For example, where the principal debtor is himself the executor, his private interests and

his fiduciary interests might conceivably conflict, and he might withhold the giving of notice to determine the guarantee, in order that further advances might be made to him on his own account, to the detriment of the estate he was administering. Likewise, where you are aware that substantially the whole of the guarantor's estate has been devised on trust it would possibly be expedient to call a halt in the guaranteed advance (*Harris* v. *Fawcett* (1873), 29 L.T. 84).

Insanity of Guarantor. On receipt of notice that a guarantor has become of unsound mind, the debtor's account should be stopped, for further advances subsequent to the notice would not be covered by the guarantee, and indeed all payments to credit would be appropriated in reduction of the indebtedness existing at the time notice was received.

In *Bradford Old Bank Ltd.* v. *Sutcliffe* (1918), 34 T.L.R. 619, it was held that, although a guarantee contained a provision that three months' notice by the guarantor or his executors was required to terminate it, this did not apply to the lunacy of the surety, and the bank could, in such a case, no longer make advances on the strength of the guarantee, for it knew that the guarantor had no longer a contracting mind. This was upheld on appeal. Any demand in respect of the guarantee would have to be the subject of representation to the Master in Lunacy.

Joint and Several Guarantees. It is hardly necessary to point out that, where two or more people are prepared to guarantee an account, it is preferable to take a joint and several guarantee for the sum in question rather than separate guarantees for a proportionate part of the total sum from each. By engaging them jointly and severally you insure against the failure of any particular surety, for each and every one of the guarantors is liable for the whole sum guaranteed; you are at liberty to proceed against one only and leave him to extract from his co-sureties their proportion of the liability.

You will notice that the guarantee of two or more parties usually makes them not only jointly but also severally liable. The principal advantage of this form of undertaking is that the death of one party—he may be the only substantial one—does not relieve his estate of liability, leaving you perhaps with one or more joint sureties of doubtful worth, whereas if the parties were only jointly liable this would be the case.

Secondly, by engaging the parties in several liability you have the utmost freedom of action if legal proceedings are necessary. If joint liability only were involved, you might find yourself in difficulties if you did not join all the parties in the action, for an unsatisfied judgment against one or more would be a bar to proceedings against the remainder. With joint and several liability, however, you can proceed against the parties *seriatim* until you have been paid in full.

When taking a joint and several guarantee it is important to obtain the signatures of all the parties before advancing money on the strength of the guarantee. Otherwise, if something occurs to prevent one of the parties signing, the others, whose signatures are on the document, may avoid liability.

In *National Provincial Bank of England* v. *Brackenbury* (1906), 22 T.L.R. 797, three persons signed a joint and several guarantee, but the fourth party died before his signature could be obtained. Although the bank had allowed the account to become overdrawn in anticipation of the completion of the guarantee, it was held that the three parties who had signed were discharged.

The death, bankruptcy, or lunacy of one joint and several guarantor involves stopping the account pending arrangements for the discharge of the liability of the party concerned, or the assent of the remaining sureties to the release of his estate. If, however, the guarantee stipulates for three months' notice from the personal representatives of a deceased surety, the account could be

continued and advice of the liability and the terms of determination given to the executors of the deceased surety.

If an account is guaranteed by two or more people severally but not jointly, by separate guarantees, the circumstances may be such that you would call from each one the full amount of his liability, notwithstanding that a proportionate payment by all would clear your debt. In such a case, you would open separate suspense accounts for each guarantor who paid, and return any excess contribution in due course. If one pays more than his quota, he has his rights against those who have defaulted.

There are two interesting points relating to income-tax that affect a guarantor in some circumstances.

You are probably acquainted with Section 36 (1) of the Income Tax Act, 1918, which permits a rebate of tax in respect of bank interest paid by a borrower. In the case of *Holder* v. *Inland Revenue Commissioners*, [1932] A.C. 624, a guarantor, who had fulfilled his liability by paying what was due from the principal debtor to the bank, claimed relief under the above section in respect of that part of the guaranteed debt that represented interest on the principal sum owing from time to time. The Court of Appeal reversed the decision of the Lower Court in favour of the guarantor, holding that the half-yearly interest sums lost their quality of interest by having become capital. The House of Lords upheld the Appeal Court's decision on the ground that interest payable on an advance from the bank meant interest on an advance made to the person paying. The guarantor did not pay interest on an advance made to him, but paid under his guarantee, his debt was his debt under the guarantee, not a debt in respect of an advance made to him. So do not give a guarantor a tax certificate in such circumstances.

But it sometimes happens that a guarantor has to ask for time to liquidate his liability, promising to keep the

interest on foot. If you transfer the guaranteed debt to him he becomes the principal debtor and any interest he, thereafter, pays can be the subject of an allowance by the Inland Revenue under Section 36.

But you may object to transferring the debt in that manner, for you thereby release your customer, who has caused all the trouble. If, consequently, the account is retained in the debtor's name, and the guarantor provides the interest on the guaranteed debt, he cannot of right claim a rebate under Section 36 of the Income Tax Act, for it is not his advance. But it is the practice of Inspectors of Taxes to exercise discretion in this respect and to recognise a bank interest certificate given to a surety in such a case.

CHAPTER V

TITLE DEEDS

> "The rule of a banker is, never to make any advances, directly or indirectly upon deeds, or any other dead security. But this rule, like all other general rules, must have exceptions, and when it is proper to make an exception is a matter that must be left to the discretion of the banker. He should, however, exercise this discretion with caution and prudence, and not deviate from the rule without a special reason to justify such deviation."—*The Logic of Banking*, by J. W. Gilbart.

GILBART'S view that advances against landed property were undesirable is not reflected in the lending activities of bankers nowadays. Even so, some modern writers have still clung to that view, notwithstanding that present-day banking practice witnesses to the contrary. Banks, while not prepared to turn themselves into building societies, are usually ready to make advances against the security of title deeds of property where there is a proper margin of cover and prospects of repayment within a reasonable time. I suppose that title deeds possess as many advantages as, and no more disadvantages than, other kinds of banking security. Land and buildings, factories and warehouses possibly excepted, are not subject to such violent and sudden shrinkage in value as, say, stocks and shares, and in normal times once a proper valuation has been made on a forced sale basis, any falling away in value can usually be anticipated and dealt with.

There are three principal disadvantages attaching to this type of security, however. Firstly, it is a more costly business for the borrower owing to stamp duties and the expenses of a professional examination of title; secondly, real property lacks the quality of ready

realisability, and delay and expense are inevitable if the banker has to dispose of his security; thirdly, there is a tendency for borrowings against property to lose their temporary aspect and to degenerate into mortgage advances.

This is why discrimination must be exercised when an advance against title deeds is proposed, for if it is evident that the proposition is best suited to a permanent mortgage it should not be entertained, or at most the advance should only be made as a temporary matter pending the arrangement of a mortgage, which you should satisfy yourself will be forthcoming, and to which course the borrower should bind himself in writing.

On the other hand, trading advances of a seasonal nature, secured on the title deeds of business premises, are a normal and proper feature of banking business.

I want it to be clearly understood that I am dealing, first of all, with unregistered land—that is, land the only title to which is evidenced by deeds and documents kept in private custody. Registered titles and land certificates will be alluded to later on.

Title deeds become security by way of mortgage, and practice differs in respect of the kind of mortgage taken—legal or equitable. In some banks the normal rule is to take a legal mortgage—an equitable charge being the exception; in other banks the equitable type prevails, legal mortgages only being taken if exceptional circumstances exist.

Yet again, at least two banks use an equitable form of charge under seal, which embodies a power of attorney in favour of certain officials of the bank, in order to make it easy for a legal mortgage to be given or for a sale to be effected later on.

Legal and Equitable Mortgages. This is possibly the time to distinguish between the legal and the equitable mortgage. A legal mortgage gives you rights against the property itself, quite apart from any personal action

against the borrower; you get what is called a legal estate in the property and you are endowed with all sorts of rights and remedies which can, for the most part, be exercised of your own initiative without seeking the aid of the Courts.

An equitable mortgage in itself gives you no rights against the property, but only a personal right against its owner—a right to participate in the proceeds of sale of the property when sold and a right to enforce your claim by invoking the aid of the Courts. In short, a legal mortgage gives you pretty well summary powers to deal with your security, while an equitable mortgage under hand depends for its enforcement on appeal to the Courts.

We will consider, first of all, the principal features of the two kinds of mortgages, and then look at the formalities to be observed in taking the security and in enforcing it. A bank form of mortgage differs considerably from the type of mortgage drawn up by solicitors for private clients, and the differences turn on the fact that a bank mortgage is not intended to be a semi-permanent form of security, as is a private mortgage. The latter is a form of investment, and frequent changes therein are not welcomed, while a bank advance, secured by a mortgage of title deeds, should possess the same quality of liquidity as is found in bank accommodation against other forms of security. Consequently, powers are taken for repayment on demand of the mortgage debt, and on default for the sale of the security with a minimum of formality.

Legal Mortgages. Firstly, let us look at the terms of a bank form of legal mortgage. The opening clause contains a promise on the part of the borrower to repay his indebtedness—the amount including interest and bank charges and relating to sums due as principal debtor or surety. The indebtedness is expressed as present and future, so as to operate as a continuing security.

The borrower likewise promises to pay all expenses

incurred in perfecting the security and in settling outgoings, such as rent, rates, taxes, insurance, and repairs. This personal covenant would give you the right to sue the borrower quite apart from the security, and in some cases it might be advantageous to obtain judgment against him on the strength of the covenant and to defer action against the security.

The second clause creates the security over the property, and, if it is freehold, the borrower in some cases grants the bank a long term of the property for 3000 years or more. One bank takes a term of 4000 years as its mortgage. If it is leasehold, the borrower will, in some cases, give the bank a sub-term of the property for a term one day short of his own leasehold interest. In other cases, the same form is used for freeholds and leaseholds and the borrower "charges by way of legal mortgage" the property as described in the schedule, instead of granting a long term or sub-term as the case may be.

Whereas before 1926 a legal mortgage of a freehold was accomplished by a conveyance of the legal estate to the lender, the borrower being relegated to an equitable interest in the property in the shape of his right to redeem it, the method under the Law of Property Act, 1925, is for the borrower to retain his legal estate—the fee simple—and to grant the lender a long term, say for 3000 years.

I would like to point out here that in pre-Act days there could only be one legal mortgage on the same piece of freehold land at any one time—for it consisted of a conveyance of the fee simple—one and indivisible—to the lender. A further lender on the same property might have his security couched as a legal mortgage, but in fact his interest was only equitable—a right to any surplus proceeds of sale.

Now, under the 1925 Act, there can be an indefinite number of legal mortgages on the same piece of land at the same time, for each successive lender can get a term

one day longer than his predecessor. I am stressing this because it has some bearing on the vexed question of searches on the Land Charges Register, to which I shall refer later.

As regards leaseholds, the law now prescribes that an assignment of the whole term cannot be given by way of mortgage, and what was an alternative method in pre-Act days is now in effect the only method—namely, the granting by the borrower to the lender of a sub-term one or more days short of the main lease.

Presumably in the interests of brevity and simplicity, the 1925 legislation prescribes a short method of mortgaging both freeholds and leaseholds by the use of the formula "the mortgagor as beneficial owner hereby charges by way of legal mortgage, etc." This short form gives the banker the same protections, powers and remedies as if he had been granted a long term in the case of a freehold, and a sub-term in the case of a leasehold. Some banks use this abbreviated form, others use the longer formula.

Then an undertaking is given as regards insurance of the security in an approved office, with power for the bank to insure and charge the premium to the borrower on any default in keeping the policy on foot. Some banks insist on the fire policy being in the joint names of themselves and the borrower or on their interest being endorsed on the policy by the company, a precautionary measure in case the borrower contrives to collect the policy moneys in fraud of the bank.

There is a possibility of trouble arising if your customer, unknown to you, effects an additional insurance on the mortgaged property; for in such a case the first company will be able to share with the second company any liability that arises under its policy. You will then be under the necessity of getting from the borrower the insurance moneys he has obtained under the second policy, and the case of *Halifax Building Society and Another* v. *Keighley*

and Another, [1931] 2 K.B. 248, shows that it is desirable to insert a clause in the mortgage deed whereby the borrower binds himself not to insure the property independently, and declares that, if in breach of the undertaking he does so, he will hold any policy money received thereunder in trust for the mortgagee and will pay it over on demand to be used in reduction of the mortgage debt. Unless this matter is specifically provided for, it would appear that a mortgagee cannot recover any moneys received under a policy taken out privately by the borrower.

A further reason for getting an acknowledgment from the company of the bank's interest in the policy is that in case of arson the company would not treat the policy as void, but would pay over the moneys due thereunder to the bank to the extent of the latter's interest.

Then there follows a series of clauses by which the borrower contracts out of those statutory rights of a mortgagor which might conflict with the bank's interests as a lender. Thus, Section 103 of the Law of Property Act, 1925, prescribes that the power of sale which is an integral part of a mortgage can be exercised only if the borrower is three months in default with his principal repayments, or two months in default with his interest payments, or has broken any of the mortgage covenants.

Now, this would appear in the case of a bank mortgage to militate against the very proper custom of having advances repayable on demand, and so you find that, firstly, the borrower covenants to repay on demand and, secondly, contracts out of his statutory right under Section 103, acknowledging in some cases the bank's right to sell without delay if demand for repayment is made and is unsatisfied.

Some banks do not take such peremptory powers, but provide in their forms for at least one month's notice to be given of their intention to use the power of sale. In practice, however, things do not move so swiftly, and a

borrower will probably find that even more latitude is extended to him than is provided for in Section 103.

Then the borrower deprives himself of his statutory power under Section 99 of the Law of Property Act, 1925, to grant leases of the mortgaged property, undertaking in some cases to get the written consent of the bank before leasing the property. You might find the prospects of a satisfactory sale seriously jeopardized if your security were found to be encumbered with a lease and the frequent instances that occur of borrowers, in the utmost good faith, granting leases in ignorance of their undertaking in the mortgage, once again gives point to my plea that, in the interests of all parties, a borrower should be warned of the disabilities under which he will labour if he executes the bank's form of charge.

Likewise, you will usually find a clause whereby the borrower contracts out of the rights given him under Section 93 of the above Act. This section deals with the doctrine of consolidation which contemplates cases where the same borrower has given to the same lender separate mortgages on separate properties.

Circumstances may arise where it makes a lot of difference to the lender if he can consolidate all these mortgages and regard them as one, refusing to release any one parcel of deeds unless the combined mortgage debt is satisfied. One mortgage may be adequately secured, while the second may be barely covered, but taking the two together, there is an ample margin. Section 93 of the Law of Property Act, 1925, is to the effect that a lender shall not be entitled to consolidate two or more mortgages and thus, if the borrower chooses to pay off the mortgage that is well secured, he may conceivably leave the lender with the other mortgage barely covered. And so the bank borrower contracts out of his right to redeem one mortgage without redeeming the lot, and thus the possibility is saved of, say, No. 1 loan, secured several times over, being redeemed, leaving the banker

with, say, No. 2 loan inadequately covered by a depreciated security. Admittedly, cases are infrequent where separate bank loans are made against separate parcels of deeds, but this clause is designed to meet such a remote occasion.

Whether different forms are used to cover mortgages by one party and mortgages by two or more, or not, it is usual to provide that in the case of a joint mortgage the liability shall be joint and several.

Some banks draw their forms so as to cover all sums advanced, or to be from time to time advanced, without limit, while others draft their charges to cover all moneys owing now or in the future, but insert a sum as the limit recoverable under the mortgage.

Equitable Mortgages. An equitable charge can be given by the mere deposit of deeds with intent to charge them, or by a written document under hand or under seal, unaccompanied by the relative deeds, giving a charge over the property in question. Of course, it is preferable to have both the deeds and a written memorandum of charge, because then there can be no subsequent dispute as to the purpose of the lodgment of the deeds.

That is why the opening clause of an equitable mortgage is usually in the form of a declaration by the customer that the deeds specified in the schedule have been deposited as security for all moneys owing at the time or subsequently. This shuts out all possibility of an assertion afterwards that the deeds were handed to you for safe custody and not for security purposes, for you will remember that a contract of that kind of bailment, known as *depositum*—an agreement to receive your customer's property in safe custody—will deprive you of any sort of lien, charge or mortgage over such property.

If you are dealing with the obstinate type of customer who is willing to lodge his deeds for the purpose of securing his advance, but flatly refuses to sign any sort of document of charge, and expediency demands that you should

indulge him, be careful not to deal with his deeds in a manner which would suggest that you waive your charge over them, such as by entering them in your safe custody records. Such a dealing with the title deeds might be interpreted as being inconsistent with the possession of any sort of charge over them. If you are dealing with a limited company in a like case, let me remind you that such a deposit of deeds with an oral charge requires registration at Bush House within 21 days of the creation of the charge by deposit.

The declaration in the equitable mortgage form is followed by a charge on the scheduled property, together with an undertaking to pay off on demand in writing all moneys owing, such moneys being expressed to cover present and future debts so as to give a continuing security, and to include interest, bank charges, and all incidental expenses. Provision for adequate insurance of the property is duly made.

The borrower also covenants to execute any necessary documents to convey the property to a purchaser, should the bank elect to use its power of sale, and further undertakes, should the bank desire to perfect its security, to execute a legal mortgage.

But I suppose it is our common experience that when things are going awry with your borrower, he is resentful of any attempt on your part to safeguard your position or to deal with the security, and you can call on him in vain to keep these covenants in the memorandum of charge. In such a case, if the document is under hand, your only weapon is the costly and tedious one of recourse to the Courts.

That is the reason why, in some cases, a power of attorney is incorporated in the instrument whereby the borrower irrevocably appoints one of your Head Office officials his attorney, to sell on his behalf or to execute a legal mortgage in his stead. As we shall see, the inclusion of this attorney clause is of the greatest

use when your customer adopts a policy of obstinate inactivity.

A memorandum of deposit containing a power of attorney has to be executed under seal, but let no one think that the seal in any way gives you any sort of legal charge—you are still an equitable mortgagee only, although powers are in your hands to acquire a legal estate in the property.

Another feature sometimes met with in an equitable charge under seal is the inclusion of a declaration of trust by the borrower, acknowledging that he holds the property charged in trust for you and empowering you to remove him from the trust and to appoint any person as trustee in his place.

This also is a helpful clause where you are dealing with a recalcitrant borrower who will not move an inch to help you in the enforcement of your security, for by executing a deed removing the borrower from his trusteeship and vesting your nominee with the property, you put yourself in a position to deal with it.

Finally, there is usually an admission on the borrower's part that there are no existing encumbrances on the property and sometimes an agreement not to create any further charge or encumbrance without the bank's written consent. If your customer happens, despite this latter clause, to create a second mortgage on the property, he cannot object if you summarily withdraw further credit facilities, for he has broken his agreement.

It may be asked: What are the respective advantages of a legal and an equitable mortgage?

It has been suggested that a legal mortgage is a more expensive and lengthy matter to prepare than an equitable mortgage; but inasmuch as, except in abnormal cases, a printed form is available in both instances, which can be filled up and executed forthwith, there is nothing to choose between the two kinds of mortgage in this respect.

It is true that the legal type incurs heavier stamping, but if you use an equitable charge with a power of attorney incorporated therein, there is no saving of duty, for the document, being under seal, requires stamping at the same rate of 5s. per cent as the legal charge. There is a saving, however, when the mortgage advance is repaid, for while the statutory receipt or surrender on a legal mortgage attracts stamp duty at the rate of 1s. per cent, an equitable charge can be receipted without stamp duty.

Of course, it must be remembered that some borrowers dislike binding themselves by way of legal mortgage for a temporary advance and prefer to give an equitable charge, which can be kept off the title.

So much for the forms of mortgage used among banks.

Investigation of Title. Now let us look at the several steps to be taken in order to perfect the security. It is the practice, unless the title is a short one deduced from a well-known local title or is free from any complications, to have a professional examination made in order to establish that the borrower is the party in whom the legal estate vests absolutely and beneficially.

But when this has been done, you are still faced with the possibility that your customer has already dealt in some way with the property, or that there are encumbrances thereon, the existence of which perchance is not ascertainable from the documents of title themselves. It is of the utmost importance, of course, to settle that you are the only mortgagee in the field, for if there are prior and conflicting interests outstanding, you may find yourself relegated to a secondary position when you come to realise your security.

Before 1926 there were definite rules for establishing the order in which competing interests in land would rank. First, priority was accorded to the legal mortgagee—remember that there could only be one—provided that at the time he took his mortgage he was unaware of other outstanding interests.

There might be earlier mortgages of an equitable nature, the deeds might relate to trust property, in which the beneficiaries had an equitable interest, but provided that the legal mortgagee knew not of these interests, he overrode them. "Where the equities are equal the law prevails" was the legal maxim.

In other words, where a number of parties had equal equities or rights in the same property, he would prevail who had acquired the legal estate in the shape of a legal mortgage, in ignorance of earlier interests and without such negligence as an omission to obtain either the relative title deeds or a good excuse for their absence.

Then suppose there was a series of equitable interests in train in the same property, in what manner were their respective priorities settled? The answer was by date order of their interests.

It was not an easy matter to determine if a mortgagee had notice of earlier interests, for it was not merely actual notice, but also constructive notice, that would operate to his detriment. Section 3 of the Conveyancing Act, 1882, said "a purchaser"—and this term includes a mortgagee—"shall not be prejudicially affected by notice of any instrument, fact or thing unless it is within his own knowledge"—that is actual notice—"or would have come to his knowledge if such inquiries and inspections had been made as ought reasonably to have been made by him"—that is constructive notice.

In other words, if there was any element present which reasonably called for inquiry and you did not probe the matter, you nevertheless were deemed to have had notice of the state of affairs which you would have found had you duly inquired.

Before 1926 it was by no means easy to ascertain when you were put on inquiry, for while certain claims on land were registrable on a public register, no provision was made outside Middlesex and Yorkshire for registering mortgages which were not supported by the relative deeds.

Of course, if a legal mortgagee got the deeds with his charge, that went a long way to demonstrate that no earlier mortgages existed, but circumstances could be imagined where a mortgagee might be given a perfectly reasonable explanation as to why the deeds were not forthcoming—they might form part of a larger estate, or other portions of land represented by them might be in the hands of another mortgagee.

So, although possession of the deeds was highly desirable, it did not shut out the possibility of earlier dealings with the land of which you might be deemed to have had constructive notice.

Now, under the scheme of mortgages, introduced by the 1925 legislation, fresh rules of priority have been evolved to fit the new order of things. There is no room for the old rule that priority is accorded to the party who takes a legal mortgage—the query might well be "which one ?" for, as I pointed out earlier, there can now be a succession of legal mortgages on the same piece of land at the same time, in the shape of a series of long terms.

So the rule is now to the effect that priority goes to the party who backs up his mortgage with the relative title deeds, and it matters not whether his mortgage is legal or equitable.

Of course, as in pre-Act days, such a mortgagee cannot take precedence over earlier interests of which he was deemed to be aware at the time, but in this connection an important restriction is placed on the doctrine of notice in that a means is provided of satisfying yourself that there are, in fact, no prior mortgages outstanding, for any lender who takes a charge over land without getting possession of the title deeds, has a means of enrolling his claim on a public register, and if he neglects this precaution he will find himself relegated to a back seat; for if you search this register and find nothing thereon, no other sort of notice, direct or constructive, will affect you.

The authority for this is found in Section 199 (1) (i) of the Law of Property Act, 1925, which says: "A purchaser"—and do not forget this word includes a mortgagee—"shall not be prejudicially affected by notice of any instrument or matter capable of registration under the provisions of the Land Charges Act, 1925, or any enactment which it replaces, which is void or not enforceable as against him under that Act or enactment by reason of the non-registration thereof."

The plain deduction from this section is that notice of an existing encumbrance may be shouted from the house tops, but if at the time of taking your mortgage you search the appropriate register and find no entry thereon relating to such encumbrance, it does not exist as far as you are concerned.

Then you recollect that I said that in pre-Act days priority as among equitable mortgagees was determined by date order of the respective charges, but this rule no longer obtains under the new dispensation, for priority among mortgagees who have not protected their security by possession of the deeds is now regulated by date order of registration on the appropriate register.

There will be no need for me to apologise for this lengthy digression if it has supplied you with the reason why, in 1926, you were faced with the new and, in some cases, haphazard practice of adding to your bundle of title deeds a search certificate issued by the Land Charges Registry.

In fine, this practice has come about because the new rules of priority put the emphasis on possession of the relative title deeds; they do not necessarily give the legal mortgagee pride of place over his equitable brother; they provide for the registration of additional interests in and claims against land which are not fortified by possession of the title deeds, and give a mortgagee the means of ascertaining once and for all, by searching, if other people have earlier claims on or rights in the property.

The added emphasis that is put upon possession of the relative title deeds by a mortgagee means that bankers are not anxious to let such deeds out of their hands save in exceptional circumstances. In the ordinary course of things you will only surrender them to a solicitor of proved repute on the written authority of the borrower and the undertaking of the solicitor to hold them on demand on your behalf as mortgagee, or to pay over an agreed sum.

In this connection, it is as well for you to stipulate that any sum so paid in shall be separately advised to you, so that you shall have prompt notice of the fact that the security is gone, apart from a credit entry in the borrower's account.

Registration of certain charges and encumbrances on land is not an innovation introduced in the legislation of 1925. Before 1926 certain claims and charges were registrable at the office of the Land Registry in London—as, for example, pending actions, annuities, deeds of arrangement and certain charges given over land under land improvement schemes, while bankruptcies were registered at the Bankruptcy Office.

Land Charges Register. The Land Charges Act, 1925, brought these various registers under one comprehensive scheme and, in addition, provided for the enrolment on the register of matters formerly incapable of registration, such as restrictive covenants, rights of way, etc., and mortgages unsupported by the relative deeds.

The corollary of registration is searching, and while before 1926 searches were not, I understand, invariably made, except possibly on the bankruptcy register, it is now the uniform practice to search against vendors and mortgagors on the unified land charges register.

The Chief Land Registrar has called attention to the unavoidable shortcomings of this register—inevitable on account of the fact that is a register of names and not of land. Any item capable of registration is enrolled

primarily against the name of the owner of the land and not against the land itself.

Names may vary in the course of time, and may be misspelt; some names are shared by such a multitude of people that a search against a name alone might be embarrassing in its results. Consequently, the Land Registrar has provided for the address of the owner of the property concerned and his description to be added. This does not absolutely identify the party concerned, for addresses change, descriptions differ, and hence the land which is the subject of the search is specified, firstly, by reference to the parish, place or district in which it is situated, and, secondly, where practicable, by a more precise description of the property by reference to the name of the road and the number of the house.

This does not meet the case of uncovered land, and consequently it is sometimes difficult to indicate precisely what particular piece of land occasions the search.

To avoid the necessity of separate searches on the five registers, a central alphabetical index is kept, wherein is entered the name, address and description of the owner of the land, the parish, place or district in which his property is situated, and, where practicable, short descriptions of the particular property which is the subject of the charge or encumbrance.

The Chief Registrar has pointed out that, while this system is inadequate and inconclusive, it has a negative value in that the mere existence of a register on which a purchaser or mortgagee may search is a deterrent to fraudulently-minded owners, who might otherwise suppress certain matters which a search would reveal.

Let us now address ourselves to the details of searching on the Land Charges Register.

Firstly, as to the method of searching. You can make a search either in person or by post, or, in cases of exceptional emergency, by telephone or telegram, which must be followed by an application on Form L.C.11. A personal

search costs 1s. per name and can be made by anyone without any authority from the estate owner. This publicity of the Land Charges Register was the subject of unfavourable comment at the time of the passing of the Land Charges Act, and is in contrast to the search against a registered title, which can only be undertaken with the consent of the registered proprietor.

It is preferable, however, to make a postal application for a search certificate, for a personal search may mean that something is overlooked, while a postal search will result in an official certificate, any errors in which are the responsibility of the Registry. By Section 17 (3) of the Land Charges Act, an official certificate of search is conclusive evidence in favour of a purchaser or mortgagee. The application for a search certificate should be made in duplicate on Form L.C.11 accompanied by a fee stamp of 1s. 6d. per name searched against.

I have already drawn attention to the inherent defects of a register of names, and so you should be careful to fill in the details on Form L.C.11 in all their available fullness. Thus the full names of the person you are searching against should be given, together with all his known addresses and his description. The general location of the property you are interested in should be added, by reference to the county and parish, place or district, former descriptions being included if the place has changed its name.

Finally, you should insert the description of the property concerned, such as its number in a certain road, or the name of the farm, etc. The resultant certificate will make mention of any subsisting entries in respect of the property mentioned on the application form, and if no details were supplied thereon, the certificate will specify any entries standing against the name searched against.

An expedited search may be made on payment of an additional fee of 2s. 6d., and you can get a reply by telephone or wire confined to a statement that there are or are

not any subsisting entries, on payment of an extra fee of 1s. 6d. This is followed by confirmation in writing—that is, a duplicate of the telegraphic reply plus the official certificate.

The search certificate shows the state of the register as at the time the Registry closes to the public—3 p.m., and 1 p.m. on Saturdays—and certificates in respect of applications received by the morning's post are normally issued at the close of business on the same day.

Secondly, as to what you are searching for. The register is divided into five parts, not all of which are of equal interest to the banker. The first is the Register of Pending Actions, whereon a party in an action pending in Court affecting land can warn the whole world of the fact, and if any purchaser or mortgagee either omits to search or ignores the entry, he will nevertheless be bound by the result of the action.

Bankruptcy petitions are, in the first instance, lodged at the Bankruptcy Office, and each day a list of such petitions is furnished to the Land Registrar, who enters them on the Register of Pending Actions, whether they are known to affect an owner of land or not. An unregistered bankruptcy petition will not affect a purchaser or mortgagee unless he had notice of an act of bankruptcy on which it was founded.

The second part of the Land Charges Register is the Register of Annuities, to which were transferred all items relating to annuities charged on land which were already registered under Acts prior to 1926. This register will be closed when all entries outstanding on 1st January, 1926, have been vacated.

Annuities created before 1926 but not hitherto registered should be found as Class E charges on the fifth register, the Register of Land Charges, and annuities created after 1925, can be enrolled as Class C (iii) charges on the same register.

The third register is styled the Register of Writs and

Orders, and such matters as writs or orders for enforcing judgments, receiving orders and that rare order—a writ of elegit—are registrable thereon. All receiving orders, whether affecting land or not, are registered here.

Then there follows the Register of Deeds of Arrangement, whereon should be filed by the trustee or any of the assenting creditors any deed of arrangement made by an insolvent debtor. Any purchaser or mortgagee will not be affected by a deed of arrangement which is not so registered unless he had express notice of it as an act of bankruptcy.

So far we have been discussing disabilities and encumbrances of which a banker would probably be aware without searching the Land Charges Register, except possibly a pending action other than a bankruptcy petition.

For example, an annuity charged on land would most probably be revealed by an examination of the title deeds of the land in question; bankruptcy matters affecting existing customers would probably have already been the subject of separate advice from the official receiver or trustee, and although non-registration of these matters might enable you to plead a sort of statutory ignorance of some of them, despite your knowledge from other sources, you would, of course, let that knowledge decide your course of action as regards your customer who was subject to such disabilities.

It is the fifth register which is of chief interest to bankers—the Register of Land Charges. This register is divided into five classes, classes C and D being again sub-divided. Classes A and B comprise certain charges acquired under various Acts of Parliament, such as the Land Improvements Act, 1864, and sundry private Acts of certain land improvement companies. They are principally given, of course, in respect of agricultural land, and are void against a mortgagee if unregistered. A feature of such charges, which is not always appreciated,

is that they take precedence over existing as well as future encumbrances of other kinds.

Thus, you may have a mortgage of a farm property, duly protected by the deposit of the title deeds, and the borrower may thereafter give a charge to one of the land improvement companies in respect of money lent to him for a drainage scheme. There is no provision made, by statute or otherwise, for the company taking the charge to obtain your consent, or to notify you as a prior mortgagee, and this later charge will have to be satisfied before yours.

This seems to be an arbitrary and inequitable business, but it is not so detrimental to the first mortgagee as it first appears. Application has to be made in the first instance to the Ministry of Agriculture and Fisheries, who will send an inspector to report whether the outlay in respect of which a charge is sought will effect a permanent increase in the yearly value of the land exceeding the yearly amount to be charged thereon.

If this is the case, the Ministry will make an order creating the charge in favour of the lending body. Consequently the reason for this inversion of priorities is that the money secured by the charge will be spent in improving your security, and hence you should be relatively better off if you should have to sell the property.

Where land with a registered title is involved, however, any claim to priority of a land improvement charge over earlier mortgages must be made in writing and entered on the register.

Class C of the fifth part of the Register comprises four classes of mortgages and charges. Firstly, there is a puisne mortgage—that is a legal mortgage not protected by the relative title deeds. You will remember that priority now goes to the mortgagee who gets the deeds, who consequently wants no further protection, while any lender who cannot for some reason get hold of the deeds can protect his charge by enrolling it—if a legal mortgage as a Class C.i charge—a puisne mortgage.

Usually such an entry will relate to a second mortgage, because the first mortgagee will, in the ordinary course, get the deeds, but it is quite possible for a first mortgagee to have a puisne mortgage, for the property charged may be part of a larger estate, the remainder of which is already charged elsewhere. Then there is a Class C.ii charge acquired by a life tenant who has cleared the estate of death duties or other charges.

Class C.iii, known as a general equitable charge, includes an equitable mortgage not protected by the relative documents of title, and should you take an equitable mortgage by way of a written memorandum only, without getting the deeds, as will usually be the case if you take a second charge in equitable form, you can protect yourself against subsequent interests by registering your document in this class. Class C.iv is called in the Land Charges Act an estate contract, and includes an option to purchase and any contract to create or convey a legal estate.

Strictly speaking, if the borrower in your equitable form of charge undertakes to execute a legal mortgage should you so desire, you can register the charge under this heading, as your customer contracts to give you a legal estate in the shape of a term of years absolute.

If your equitable mortgage is backed up by possession of the deeds you have all the necessary protection, and there is no point in registering as a C.iv charge.

Class D charges are of three kinds. D.i is a charge acquired by the Inland Revenue for death duties. Before 1926 it was a tedious business to satisfy yourself that no death duties affecting the land were outstanding; but now, if a search on the Land Charges Register reveals no entry in this respect, you are under no duty to inquire further. I understand that it is not the normal practice of the Inland Revenue to register charges for death duties, as they rely on following the proceeds of sale for satisfaction thereof.

Class D.ii is a restrictive covenant created after 1925.

Such restrictions on the use of land may seriously affect its value.

Similarly D.iii charges concern equitable easements, such as rights of way, light and drainage. The existence of a right of way might likewise have an adverse effect on the value of your security.

The fifth class, E, comprises annuities created before 1926, but not registered before that date.

Assuming you have made your search, and, instead of the familiar certificate marked "no subsisting entries," you find one of the foregoing charges noted thereon, you should ask on form L.C.14 for an office copy of the entry, which can be obtained for 1s. 6d. Your action will then be dictated by circumstances. If the entry is of a mortgage variety—Class C—you have got that notice of prior rights which will relegate you to second place, even if you have got the deeds.

It may be, however, that you have got in your possession this particular mortgage duly discharged by statutory receipt or otherwise, in which case you may ignore the entry, for its registration merely gave notice of the charge to future purchasers or lenders, and if the mortgage debt has been duly satisfied, neither the borrower nor the mortgagee is bound to get the entry vacated.

I suppose the most frequent entry revealed by a search certificate is class D.ii, a restrictive covenant. Whether you will follow this up or not depends on the type of property you propose to lend against.

If it is old-established residential property, you possibly will not trouble further, but if you are concerned with a building estate it is expedient to get an office copy of the entry, for your advance may be for the purpose of erecting a type of building in breach of the covenant.

Likewise, where you are dealing with business property, or private property to be used for professional purposes, you should satisfy yourself that the borrower's use of the property will not be contrary to the covenant.

So much for the method of searching and the objects of your search. Now let us consider the question of the time of searching. You will appreciate that it is of the greatest importance to search at the right time, so that when you complete your purchase, or lend on your mortgage, you can be assured that no adverse entries are on the register.

Solicitors found it an awkward matter, after the passing of the Land Charges Act, to search on the very day of completion, and so the Law of Property Amendment Act, 1926, lays it down in Section 4 (2), as amended by the Land Charges Rules, 1940, that where a purchaser has obtained a search certificate, and completes his transaction within fourteen days after the date of the certificate, he shall not be affected by any adverse entries, not made pursuant to a priority notice, registered during those fourteen days. This gives a solicitor breathing space.

The term "purchaser" in all the Property Statutes expressly includes "mortgagee," and so if a banker were advancing a sum by way of loan or overdraft he would be safe if he searched and got the mortgage form signed not later than the fourteenth day after the date of the search certificate.

In the case of an ordinary non-banking mortgage, if the lender is asked to advance a further sum, unless he is bound to do so by the terms of the mortgage, he must search again before so doing to see if, since the date of his last search, the borrower has created a charge elsewhere on the property.

Special provision has been made for fluctuating advances such as a banker makes in the legislation of 1925 and 1926.

A fluctuating overdraft secured by a mortgage of deeds is nothing but a series of advances, and if the above rule were to apply to a banker's mortgage by way of fluctuating overdraft, he would have to search before he paid each cheque. The framers of the 1925 legislation realised this and catered especially for the banking

advance in Section 94 (2) of the Law of Property Act as amended by the following Act of 1926.

The combined effect of these enactments is that where a mortgage is taken expressly to secure a current account or other further advances (such as a fluctuating loan account), the banker is not affected by any mortgages appearing on the register subsequent to the time when the original mortgage was created or to the date of the last search, whichever is the later date.

Thus having once searched, a banker can only be affected by direct notice of a second mortgage, unless for any reason he chooses to search again.

It is not always appreciated, however, that this concession to bankers only covers the case of subsequent registration of *mortgages*, and consequently the subsequent registration of any other item, such as a pending action, writ, bankruptcy petition or receiving order, would be actual notice to a banker. The risk, however, is remote in the case of receiving orders, for the Official Receiver is usually very prompt in advising a banker of bankruptcy matters.

But since the coming into force of the new legislation one bank has suffered loss as a result of the registration of a pending action, as the bank's claim over the security was determined as from the date of such registration, although they were unaware of it, and consequently lent further sums. This is no new risk, however, for such matters as pending actions, annuities, writs, etc., were capable of registration before 1926, and one can only rely on the probability that direct notice will be given of such matters in addition to notice by registration.

Frequently a banker advances money to assist a customer in buying a property and the bank's solicitor sees the transaction through, handing over a draft for the purchase money against delivery of the deeds. In a good many cases, while a search is made against the party who is selling to your customer, no search is made against

your customer, on the ground that, as the deeds have come straight to you from the vendor and have never been in your customer's hands, he cannot very well have created a prior charge over them. But in point of fact he could have done this by giving a charge to a party who was prepared to lend without getting the deeds, and who protected himself by filing a priority notice on the register. This is a method provided by the Amendment Act of 1926, as amended by S.R. & O. (1940) No. 1998, whereby at least fourteen days before he actually gets his mortgage a prospective mortgagee can give a preliminary notice of his intention to register a charge.

Thus, although the possibility of your customer having already charged the property he is buying is so remote as to be scarcely worthy of serious thought, you should search against him as a matter of formality so as to ensure that no priority notice stands in front of you.

A further point in practice arises where property has changed hands more than once since 1925. You will, of course, search against your customer, the present owner, but must you see that search certificates are present in respect of every name in which the property has stood since 1925? As a counsel of perfection the answer is "yes," but in practice it is not done.

Assuming that the official search predominates in practice over the personal search, there should be few missing certificates in a title which has changed hands frequently since 1st January, 1926, and in view of the smallness of the search fee, it would appear better to search where there is no certificate than to assume that a search was duly made.

The *Solicitors' Journal*, Volume 76, at page 215, states that the banking practice of requiring certificates in respect of every change of ownership is reasonable and prudent, but points out that the additional protection gained is possibly not worth the trouble and expense. Emmet, in *Notes on Perusing Titles*, says: "As registra-

tion is now notice to all the world, certificates of search become a very important part of the title.

"As regards any missing certificates, the purchaser (or mortgagee) cannot raise any objection. It only remains for him to consider how far it is necessary to fill up the gap by obtaining certificates himself. But the solicitor should get his client's authority if he omits to make any searches. Otherwise he might become personally liable."

If you have an equitable mortgage and succeed in getting your customer to execute a legal mortgage later on, a further search should be made. Likewise, if you take an additional charge over the same property, as happens if you use limited charges, you must make a fresh search, and if your form is drawn to cover all advances without limit and you take an additional form in an attempt to regularise the stamping position, I think, as a matter of precaution, a further search should be undertaken.

Other Searches. There are other public registers, however, besides the Land Charges Register, which may require searching according to circumstances.

Under the Land Charges Act, 1925, local authorities were empowered to set up registers for the purpose of recording certain charges acquired by them over land within their jurisdiction. Thus, if under the Public Health Acts a local authority serves notice on the owner of property to put it in order and he defaults, it can undertake the work itself and the cost thereof is a first charge on the premises and can be so registered.

Likewise, expenditure incurred on making up roads and laying down drains will be chargeable on the property and will be registered on the local register. Then special classes of restrictive covenants created by local authorities, such as town planning schemes and other restrictions on the use of land and buildings, are enrolled on these local registers.

Unlike the Land Charges Register, they are concerned with properties, and not proprietors. The cost of a

personal search of all parts is one shilling per parcel of land, while an official search certificate will be issued covering the whole register for 5s.

There is no uniformity of practice in searching the local registers, in addition to the Land Charges Register, and possibly they are ignored where old-established property is concerned. But if you are dealing with newly-erected properties or building estates, I suggest that searches are highly desirable, for road charges may have to be met, the district may be subject to a town planning scheme, or certain restrictive covenants may have been imposed by the local authority.

If it is deemed necessary to search, you will not have done all that should be done unless you search not only the registers kept by the urban, rural or borough council, etc., but also the register of the county council, so you will see that searching is a costly matter—here a little and there a little—but it is better to have searched them all than never to have searched at all.

Then you may be concerned with property in Yorkshire.* This county possesses Deeds Registries over two centuries old, the purpose of which is to provide a handy record of all documents relating to the ownership of land, useful if deeds are destroyed or defaced, and a deterrent against fraudulent duplication of documents of title. These registries are not concerned with titles, but with documents, and must not be confused with the system of registration of title as obtains in London, Middlesex, Eastbourne, Hastings, and Croydon.

If you are dealing with property in Yorkshire you must search the Deeds Register of the particular Riding, primarily for any legal mortgages, puisne or otherwise, and also for any equitable charges protected by the respective deeds, for equitable interests can still be registered in Yorkshire.

The new legislation provided for the institution of

* The City of York is outside the Yorkshire Deeds Registries.

Charges Registers in Yorkshire for the enrolment of such matters as easements, covenants, estate contracts, and equitable charges not supported by deeds. Accordingly, such items affecting Yorkshire land are not now registrable on the London Land Charges Register, and so in addition to searching the Deeds Register you should also search the Charges Register, particularly for any equitable mortgages outstanding that are not protected by the title deeds.

Thus, the Yorkshire Register is practically self-contained, and there is no need to search the London Land Charges Register unless you have reason to suspect that one of the very few items that are registrable there instead of in Yorkshire is encumbering the property in question. Once again, you must use your discretion where Yorkshire land is concerned as to whether you search the Local Land Charges Register also. You will, of course, search the register kept by the local authority in appropriate cases.

Until 1937 there was a similar Deeds Registry in respect of the County of Middlesex. These were closed for registrations, however, when this County was made a compulsory area for land registration with effect from 1st January, 1937. Facilities for searching the Deeds Registers, however, were still available until 1940 when the registers were finally closed under the Middlesex Deeds Act, 1940. In 1943, however, the registers were reopened for searches, only in cases where deeds and documents had been destroyed by enemy action, to assist in reconstituting titles. For this purpose, the registers are housed at the Middlesex Guildhall, Westminster, and the County Hall, Westminster Bridge.

When taking a mortgage from a limited company over its land and buildings, the primary search should be made at Bush House, where particulars of any debentures and any charges on land, whether accompanied by the deeds or not, are enrolled. The search must be a

personal one, as no certificates of search are normally issued by the Registrar. If you find that any debentures are outstanding, you should ascertain beyond all doubt that the property which is being mortgaged to you is not the subject of any sort of charge in the debenture.

To save dual registration, Section 10 of the Land Charges Act provides that a land charge given by a company is sufficiently protected by registration at Bush House and has the same effect as if registered on the Land Charges Register. Thus, there is no need to search the latter register for a legal or equitable mortgage not protected by the documents of title.

But if you wish to make certain that there are no other disabilities attaching to the property which you are taking as security, you should search the Land Charges Register in the usual way for such matters as pending actions, writs, restrictive covenants, etc. You will also have to search the deeds registries of Yorkshire if you are concerned with land in this county, and, if circumstances make it desirable, the registers of the County and Local Authorities.

Town and Country Planning Act. When title deeds are taken as security after June 30th, 1948, it will be necessary to find out if any development in the property concerned has taken place since that date. If such be the case, a sight of the planning permission should be obtained, together with the Central Land Board's certificate that the development charge has been paid by the borrower. If a customer lodges as security the title deeds of land which he proposes to develop, inquiries should be made as to whether sanction to develop has been obtained and as to the position regarding payment of the development charge.

Making the Advance. We will assume that you have got your mortgage form signed and your search certificate returned with no entries thereon—can you safely make the

advance without further ado? In most cases the answer is "yes," but in some cases registration is required in order to perfect your security. If you are dealing with unregistered land outside Yorkshire, and you have followed the normal course of getting the title deeds, you have no need, apart from limited companies, to register, for, as you will remember, you have got the maximum of security.

If, however, you have to take your mortgage without the deeds for some reason or other, you must register your charge as a puisne mortgage, or a general equitable charge, according as it is a legal or equitable document. This will be done on Form L.C. 4 at a fee of 1s. per name, and to prevent frivolous registrations the application must be supported by a statutory declaration unless lodged by a solicitor. The Registrar will issue an acknowledgment of the application, which should be carefully filed with your security, for the date of registration regulates your priority.

Sometimes you have some deeds, but not all the material ones relating to the title—in such a case it is advisable to register; and, in this connection, it must be noted that the Registrar is not concerned with the regularity of any entry—he does not require to see the original deed or instrument creating the charge which you are registering.

If you are dealing with Yorkshire land, you must enrol a legal mortgage, whether supported by the deeds or not, at the Deeds Registry of the respective Riding. If it is an equitable mortgage without the deeds, you must enrol it on the Yorkshire Charges Register; if you have the deeds with your equitable charge you could register on the Deeds Register as a matter of expediency.

If the borrower is a limited company, your charge of whatever kind must be registered at Bush House within 21 days of its execution, and a certificate of registration will be issued as evidence thereof Oral charges—

that is, charges created by the mere deposit of the deeds with intent to charge—should be registered. Whereas the effect of non-registration on the various registers of charges given by non-company customers simply means that you jeopardise the priority of your security, non-registration at Bush House of any charge over land given by a limited company has far more serious consequences, for it is void as against a liquidator and you are relegated to the position of an unsecured creditor.

Second Mortgages as Security. If you have to take a mortgage without getting the relative deeds in your possession it will usually be because they are already charged elsewhere—in other words, you have a second mortgage as security. Such security is naturally not liked by bankers unless there is an undoubted and considerable difference between the value of the property and the amount of the first mortgage. It is not unusual to find that the equity disappears on account of shrinkage in the value of the property or drastic action on the part of the first mortgagee, resulting in an uneconomic sale being forced.

When you are casting round for any form of cover to bolster up an unsatisfactory advance, you often have to fall back on the doubtful expedient of a second charge. In this and in all cases where you are not going to get the deeds to support your charge, you should take a legal mortgage rather than an equitable one, for it is possible in some circumstances for an equitable charge to be overridden even if registered.

You should, when taking a second charge, in addition to any necessary registration, give notice of it to the first mortgagee and get his acknowledgment, for if his mortgage is framed to secure further advances he will not be under the necessity of searching before increasing his mortgage advance, and hence may continue to lend to the detriment of your security. When taking the second

charge you should ascertain if the first mortgagee is bound by the terms of the mortgage deed to make further advances; for example, if the mortgage speaks of £1000 and he has lent to date only £500.

In such a case he can make further advances despite notice of your charge. If this is not the case, a first mortgagee must make no further advances on the strength of the mortgage after receipt of your notice of second charge unless you consent.

Notice of Second Mortgage. Having got your mortgage executed, made the necessary searches and effected any necessary registrations, you can safely make the advance, and remember that as long as you do not make a further search you are not in any way affected by registrations of any subsequent mortgages on the Land Charges Register. But if, after the making of your advance, you are served direct with a notice of a second charge, you must break the account in order to establish the amount for which your first mortgage will avail.

If the account is continued on an unbroken basis, the operation of the rule in *Clayton's* case will result in subsequent credits to the account being applied in reduction of the debt existing at the time notice was received, and all further debits will be in the nature of fresh advances postponed to the second mortgage.

This was laid down decisively by the House of Lords in the much-quoted case of *Deeley* v. *Lloyds Bank, Ltd.*, [1912] A.C. 756, where the doctrine known as the rule in *Hopkinson* v. *Rolt* was applied—namely, that where there is a mortgage to secure further advances the mortgagee cannot obtain priority for any advances made after notice of a subsequent encumbrance.

Once you have got your mortgage completed you are not affected by the subsequent registration of other mortgages unless you choose to search, but you cannot ignore direct notice of any such charges.

If your customer gives a second charge over your

security you are released from any obligation to honour further cheques on the strength of such security, for he has himself limited the amount you may advance against it. An interesting position arises where the advance is by way of loan and notice of second charge is received when a credit balance exists on the current account.

The advice tendered by Sir John Paget to the Institute of Bankers is that the loan account should be broken and interest charged to date, but that the customer is entitled to deal with his credit balance on current account. This, of course, is the case where the document of charge refers specifically to a loan of named amount, but where a charge is drawn to secure all moneys on all accounts it has been contended that, to get at the amount for which the security is available, the banker must combine the loan and current account.

If a borrower has agreed in your form of charge not to create any further encumbrances on the security, you could use this breach of covenant as a reason for calling for repayment of the loan, and thus obtain the right to appropriate the current account balance. I imagine, however, that you would be chary of returning such a customer's outstanding cheques, drawn in reliance on the credit balance, without giving him due notice of your intention to combine the accounts. Possibly the safest plan would be to get an acknowledgment from the second mortgagee that your security covers the full amount outstanding on loan account.

Occasionally you receive notice of a second charge which specifically mentions that it is subject to an advance by you of a named amount. If your advance is by way of overdraft, however, you should be careful to see that the notice of second mortgage makes it plain that you are free to make advances by way of fluctuating overdraft to an amount not exceeding at any one time the named sum.

There is another case where you might be under the necessity of breaking the account in order to establish

the amount for which you can hold your security—where the borrower has sold the property. Notice of this fact may be as significant as notice of a second mortgage, and if it happened that the purchase money was paid by instalments, you might find that when the purchaser was at last entitled to call for a conveyance, your security was gone, in that payments into the account since you had notice of the contract for sale had been sufficient to wipe out the debt existing at that time. The case of *London and County Banking Company* v. *Ratcliffe* (1881), reported in Vol. I of *Legal Decisions Affecting Bankers*, is worth studying in this respect.

Questions sometimes arise as to whether the party offering title deeds in his own name as security is merely a nominee—a trustee holding the property for a beneficiary. The legislation of 1925 was somewhat arbitrary on the subject of secret trusts, but the Amending Act of 1926 in the Schedule of minor amendments makes it plain that so long as the title deeds of the property are produced and you have no notice of any fiduciary interest of your customer, you are entitled to deal with him as beneficial and absolute owner.

In other words, mere suspicion of a secret trust is not enough, you must have some sort of notice of it, express or constructive. I suppose the matter mostly arises where husband and wife are concerned. If your customer borrows in his own name for the purpose of building a house which is to be conveyed into his wife's name, it would appear desirable to inquire if she is going to be a nominee for her husband or if the latter is taking no beneficial interest in it. The best way out of the difficulty is to get both parties to execute the form of charge.

Very occasionally, when an advance against deeds is transferred from one bank to another, a transfer is taken of the first bank's mortgage—that is, the form of charge is handed over, together with a deed of transfer, instead of the mortgage being discharged and a fresh form of

charge being executed in favour of the bank to which the account is transferred. A certain amount of stamp duty will be saved by this procedure.

You should be careful to see, however, that the borrowing is now taken on a separate loan account, on which the only operations should be reductions, for the transfer of the advance fixed the amount for which the first bank's mortgage could be held by the second bank, and all payments to credit will go in reduction of the debt existing at the time of the transfer of the account.

You are sometimes offered a sub-mortgage as security, that is to say your customer has lent money on mortgage and now in turn wishes to raise money, not on the property, but on his mortgage of it. He may charge the mortgage deeds on one of your standard forms, either as a legal or equitable charge, and you should, of course, get not only his mortgage deed, but the deeds of the mortgaged property.

You should give notice to the mortgagor—the original borrower —so that any instalments of the mortgage debt are paid to you and not to your customer, the mortgagee. You should ask for an acknowledgment of your notice, stating the amount outstanding. There is no need to search against the mortgagor, assuming that this was done when the mortgage was taken, but possibly you should search against your customer, the sub-mortgagor, to see if he has already sub-mortgaged your security without yielding up the deeds.

It is by no means certain that sub-mortgages taken without the deeds are capable of registration on the Land Charges Register—there is no reference thereto in the Land Charges Act. If such a charge was offered for registration, it would probably be accepted, as the Registrar is not concerned with documents and the instrument would presumably be registered as a Class C.i or C.iii charge. Hence, search against your customer as sub-mortgagor.

Repayment of Advance. The question now arises as to your procedure if an advance secured by a legal mortgage of title deeds is repaid by the borrower. Something has to be done to show that the mortgage is at an end, to free the property from the mortgage encumbrance. Before 1926 a reconveyance or surrender had to be executed because a legal mortgage was effected by a conveyance of the legal estate to the lender, and this legal estate had to be put back into the borrower's hands.

A legal mortgage is now discharged by the giving of a receipt for the mortgage moneys, usually endorsed on the back of the form of mortgage, and this has the effect of extinguishing the mortgage term. This statutory receipt must be expressed to be for all moneys secured by the mortgage, or for the balance owing, and it must give the name of the party paying the money.

In the absence of other provision, where the money is not expressed to be paid by a party entitled to redeem the mortgage—that is the original borrower or his transferee—the receipt operates not as a discharge of the mortgage but as a transfer of it.

Although there is nothing in the Law of Property Act to the effect that a statutory receipt must be under seal, it is the custom to have it sealed by the bank. If the borrower so desires, however, he can have the mortgage discharged in the old way by a surrender, release or reconveyance. This method is generally used where more than one property has been charged on one form and one only is being redeemed.

There is yet another way of extinguishing the mortgage term, found in Section 116 of the Law of Property Act—by a plain receipt given under hand. Provided this does not contain any words purporting to release the property from the mortgage it will not require stamping. If a statutory receipt is used stamping will be required at the rate of 1s. per cent on the highest amount secured by the mortgage.

If your mortgage is in equitable form, however, no statutory receipt is required and a simple acknowledgment of the receipt of the mortgage moneys given under the hand of a head office official is all that is required. Such a receipt does not attract stamp duty as it falls within exemption 11 of the schedule to the Stamp Act, 1891.

If you are concerned with an equitable mortgage containing a power of attorney, and hence under seal, you will find that a good many solicitors like to have a duly stamped and sealed statutory receipt. There seems to be no authority for this, for the mortgage, although under seal, gives no legal estate and is of an equitable nature only. Possibly as an act of grace, or to avoid delay in getting your money, you will give a statutory receipt, but this is a matter of expediency, and not of law.

Before surrendering the deeds of mortgaged property to a borrower who has cleared his debt, is a banker under any duty to search the Land Charges Register to see if anyone else has an interest in the property? The Law of Property Amendment Act, 1926, has dispelled any ambiguity on this score and made it plain that no such duty exists, for it amends Section 96 (2) of the principal Act to read "a mortgagee whose mortgage is surrendered or otherwise extinguished, shall not be liable on account of delivering documents of title in his possession to the person not having the best right thereto, unless he has notice of the right or claim of a person having a better right. In this subsection notice does not include notice implied by reason of registration under the Land Charges Act, 1925, or in a local deeds register." Of course, if you receive direct notice from a second mortgagee, you must not deliver the deeds to the borrower but hold them in trust for the second mortgagee.

A frequent happening, however, in banking practice is for an advance secured by deeds to be repaid by the sale of the property by the borrower, probably as a result of discreet pressure from the banker. In such a case, if there

are any surplus proceeds, should the banker search to see if there is anyone better entitled to them than the borrower?

I believe that opinions differ on this point, but it appears to me that no risk is run in placing the surplus proceeds at the disposal of the borrower, unless you have had direct notice of a second charge; you need not search, for in point of fact you are not exercising any power of sale—you are handing the deeds over to a nominee of your customer against payment.

We have now to consider the unsatisfactory occasions when a banker is compelled, in order to clear his customer's indebtedness, to put into force the various statutory powers given to a mortgagee. Before you avail yourself of these remedies, however, the borrower must, of course, be in default. This arises when formal demand has been made on him and no satisfaction results. In some bank mortgages it is provided that the remedy of sale shall not be exercised until one month's notice has been given of the bank's intention so to do, while in other cases it is provided that the power of sale shall be exercisable directly default is made.

But in all cases, I imagine, the borrower is shown every latitude, and an unsuccessful demand by the bank is usually followed by a solicitor's letter reminding the borrower of the effect of default.

Remedies of Mortgagee.* There are five remedies available to the legal mortgagee, and they can be exercised singly or together. Firstly, the banker, as legal mortgagee, can sue on the personal covenant to repay, which is the preliminary clause in bank mortgage forms. More usually, of course, you sue for the amount due on the banking account.

A writ is the weapon to use where you know that the

* At the present time (1950) the Emergency Legislation of 1939 is still in force whereby the leave of the Court must be sought before a mortgagee can avail himself of the powers to deal with his security.

borrower is possessed of means and there is some doubt if the disposal of the security will result in the liquidation of the entire indebtedness. In such a case you will normally get judgment, which, if unsatisfied, will give you further rights to exercise—the usual one being the issue of a bankruptcy notice with its sombre prospect for the obstinate debtor.

The next course open is to sell the security, and this, except in the case of an equitable mortgage under hand, does not entail application to the Court. The right of sale is inherent in a legal mortgage and is exercisable after default has been made and notice given in accordance with the terms of the mortgage instrument. This is the advantage which a legal mortgage possesses over the purely equitable variety—your remedy lies to your hand forthwith without further formality.

There is no need for you as mortgagee to put the property up to auction in order to get a representative price—you are at liberty to sell by private treaty if you so desire (Section 101 of the Law of Property Act). Prudence demands, however, that you should get the consent of the borrower or a professional valuation. It is a sound banking custom to instruct estate agents, or auctioneers, that the bank's name is not to appear in any advertisement of sale—for there is an impression in some circles that banks are fair game and will be prepared to sell at a bargain price in order to rid themselves of an embarrassing security.

You must conduct the realisation of the mortgaged property as a reasonable person would behave in the realisation of his own property, and must not wilfully or recklessly sacrifice the property. In practice you usually invite any second mortgagee to take over your mortgage before you proceed to sell.

Assuming that you have effected a sale, the subsequent conveyance can be sealed by the bank without bringing the customer into the business, and such conveyance will

give the purchaser a valid title free from any second or subsequent mortgage that may be outstanding. Section 104 of the Law of Property Act, 1925, makes this clear: "A mortgagee exercising the power of sale . . . shall have power by deed to convey the property sold . . . freed from all estates, interests and rights to which the mortgage has priority, but subject to all estates, interests and rights which have priority to the mortgage."

You may say: "How about the unfortunate second mortgagee who sees the property being conveyed away regardless of his interests?" The answer is that he must follow the proceeds of sale in the hands of the first mortgagee, for the next section of the Act provides that such proceeds shall be applied by the mortgagee who is selling in payment of the costs of sale, in discharge of the mortgage money and interest, and the residue shall be paid to the person entitled to the mortgaged property—that is, the second mortgagee.

So in the happy but unlikely event of any surplus accruing after you have cleared your books, you must hold it in trust for the person entitled to the mortgaged property. Any surplus proceeds of sale must not be credited to your customer's account until you are sure that no other mortgages are outstanding. If there happens to be a second mortgagee you will probably have had direct notice from him. If a foreclosure order absolute is obtained, however, as is explained later, you are not accountable to anyone—the property becomes yours absolutely.

But do not let absence of notice lead you to pay over any surplus to the borrower—you must search the appropriate registers to see if there is a puisne mortgage or general equitable charge registered against your customer.

If you are a second mortgagee, anxious to liquidate the mortgage advance, you are quite entitled to sell without the first mortgagee's permission, but what will probably deter you is the difficulty in obtaining a price that will

clear off the first mortgage and also wipe out your debt. You will recollect that the section I just quoted makes it plain that any sale by a mortgagee means that the proceeds of sale are "subject to all estates, interests and rights which have priority to the mortgage."

A difficulty that frequently arises where your security is a dwelling house in the occupation of the borrower, and your power of sale has arisen, is that a sale is held up because your customer will not quit the premises and enable you to give vacant possession. Unless you adopt the tedious and lengthy course of an order for foreclosure, matters are likely to remain at a standstill, and that is why occasionally you find a clause in a legal mortgage whereby the borrower attorns tenant to the bank at a peppercorn or other nominal rent, with a proviso that such tenancy does not constitute the bank a mortgagee in possession so long as the borrower remains in occupation of the premises.

If your customer refuses to give possession of your security after your power of sale has arisen, you are then able to apply to the Court on a specially endorsed writ for possession under Order 14, and an order to this end will be granted unless the borrower can put up a convincing defence. If you have not got this attornment clause in your mortgage form, and you do not want to embark on the lengthy procedure of foreclosure, you can apply for an order for sale with possession, which in some cases will be granted very much more quickly than a foreclosure order.

Another remedy of the banker as mortgagee is to appoint a receiver of the income of the mortgaged property. This step is taken in cases where a sale is impracticable because the premises are let, or where entire repayment of the advance is not likely to result from a forced sale, but may be possible if you care to await an improvement in the property market.

In a good many instances a sale with possession is

practically out of the question, and then a bank must perforce hold its hand until the tenant's lease has expired. Meanwhile, in order to get hold of the rents of the property, the bank appoints a receiver—usually the branch manager in straightforward cases, otherwise a professional man who is an expert in such matters. The receiver's authority will be a document usually under the seal of the bank reciting the details of the form of charge and stating that the borrower is in default. Production of this to the tenant of the property will mean that all further payments of rent must be made to the receiver.

The main idea of appointing a receiver is to keep the mortgage interest on foot by appropriating the rent to that end. Such income must be applied, firstly, in discharge of such outgoings as taxes, rates, insurance, repairs, etc.; then in payment of interest on the mortgage debt; and, finally, any residue must be used in reduction of the debt itself—a new provision, but one which in practice does not always benefit the banker, who is lucky if, after having satisfied outstanding items for rates, repairs, etc., he finds a sufficient surplus available for interest on the advance.

Another course open to the banker as legal or equitable mortgagee is to apply to the Court for an order for foreclosure—a lengthy business, for the Court will usually make an order *nisi*, which will not become absolute until six months have elapsed without the borrower having paid up the principal and interest due. The order absolute has the effect of depriving the borrower of his equity of redemption, and vesting the entire interest in the property in the lender, who can sell if he so desires and retain the entire proceeds without regard to any surplus that arises. This remedy is not normally exercised by a banker.

The last remedy is to enter into possession of the mortgaged property—technically, this can be done at any time during the currency of the mortgage, for you have a lease of the premises in the shape of a mortgage term;

but in practice it is rarely done at all, even when the borrower is in default, for there are onerous obligations attached to such a step. For example, if you enter into possession, you must account not only for the rent and profits issuing from the property, but also for the revenue you might have received if you had used due diligence.

So much for your remedies as a legal mortgagee—what of your rights if you have only an equitable charge under hand and the time has arrived to enforce your security? Unless you can induce the borrower to sign a legal mortgage, in accordance with the covenant in the equitable charge—and experience testifies to the dogged obstinacy of borrowers in such circumstances—your only recourse in respect of the security is to apply to the Court for an order for sale, or an order for foreclosure and sale, or for the appointment of a Receiver of Rents. You can resign yourself to a costly and lengthy delay in such a case, possibly involving you in missing the market for your security.

If you have used an equitable form of mortgage embodying an irrevocable power of attorney, however, your weapons are pretty well as effective as if you had a legal mortgage. The inclusion of a power of attorney means that the mortgage must be executed under seal and, to start with, you can appoint a Receiver of Rents without the formality of an application to the Court and without reliance on the power of attorney. For Section 101 of the Law of Property Act states that where the mortgage is by deed the mortgagee shall have power to appoint a receiver.

Under the same section, where the mortgage is by deed you have a power of sale, but you cannot give a purchaser a legal estate, as you yourself have only an equitable one. So if you wish to dispose of your security charged under this type of mortgage, you employ the fiction of selling not as mortgagee, but as attorney of the borrower. In such cases the conveyance will usually recite the power of attorney given in the charge, and the bank as mortgagee, and it will be executed in due form by a head office official

as attorney for the customer, and sealed by the bank as mortgagee.

If the borrower is in occupation of the property and will not budge, and you have this equitable charge with a power of attorney therein, you can first of all turn your equitable mortgage into a legal one containing an attornment clause * by the simple expedient of getting one of your designated officials to sign and seal the legal mortgage as attorney for the borrower, who has covenanted in the equitable charge to give you a legal charge. You are then at liberty to go ahead under Order 14 with a specially endorsed writ for possession.

There is yet another method of enforcing your power of sale under an equitable form of charge under seal, and it is available where a clause is included by which the borrower acknowledges that he holds the property in trust for you and authorises you to remove him from the trust and to appoint another in his place. This enables you to execute a deed appointing one of your officials as trustee in the borrower's place, and thereafter he can give a valid title to a purchaser.

In these days, unfortunately, there is an increasing number of borrowers who have to seek a solution of their troubles in the Bankruptcy Court. If you happen to hold title deeds as security, it is not likely that the trustee in bankruptcy will redeem them and you will have eventually to sell your security. Section 110 of the Law of Property Act provides that if a power of sale arises solely on account of the borrower's bankruptcy, the leave of the Court must be obtained.

This does not mean that before you can sell the deed security of every bankrupt borrower you must get the permission of the Court, for you will call up your power of sale by serving the usual demand for repayment, and sell as a result of default following such demand.

If you are going to be left with a provable debt after

* See p. 158.

having disposed of the security, you should get the trustee's approval of the sale; and if you have actually proved, after assessing the value of your security, you must not forget that the trustee has certain rights of redemption over the security, which may limit your selling powers.

If your mortgage is equitable in form, unless you make application to the Court for an order for sale, you will have to get the trustee in bankruptcy to join in the execution of any conveyance following a sale of the property, but if your equitable mortgage contains an irrevocable power of attorney it is possible to sell without the trustee's co-operation. Section 126 of the Law of Property Act says that in favour of a purchaser, such a power shall not be revoked by the death, disability or bankruptcy of the donor of the power, and hence your power of attorney can be validly exercised in favour of a purchaser.

While in some quarters this interpretation of Section 126 is not accepted, it would appear from Sub-section (1) that for the purpose of conveying to a purchaser the question of bankruptcy can be disregarded in so far as the exercise of the power by the donee is concerned.

This section is also of avail where you are concerned with a deceased borrower whose deed security was charged under an equitable form containing a power of attorney. If no one is moving to administer the estate on account of insolvency, for example, it is an expensive business for the bank to apply for a grant of administration in order to sell the security, and this can be avoided by the exercise of the power of attorney, which, as far as a purchaser is concerned, is not revoked by the donor's death.

Then there is the vexed question of interest in bankruptcy. If you propose to rely on your deed security for entire repayment, you are at liberty to recoup yourself from the proceeds of sale, not only for principal and interest up to the date of the receiving order, but also for subsequent interest up to the date of payment.

But if you are going to prove on the borrower's estate

because, for example, the realisation of the security leaves you with a portion of the advance unsatisfied, you can only claim interest up to the date of the receiving order, unless, of course, the debtor's estate yields any surplus when wound up. But if you have put in a receiver of rents, you are able to appropriate the income from the property as interest on the debt after the date of the receiving order.

CHAPTER VI

REGISTERED LAND

There are four main qualities which should characterise a perfect system of land ownership and transfer.

Firstly, it should be secure, and this means, among other things, that a purchaser of land should be assured of an unassailable title and should not be confronted with conflicting and undisclosed interests at a later date. Then there should be some measure of security for successive lenders of money against land, so that they should know the order in which their rights against the property are marshalled. Then there are the rights to be safeguarded of parties who have no ownership of the land, but interests therein, such as lessees and owners of easements and covenants; lastly, there should be an element of security in that documentary proofs of title should be secure from loss, duplication, or destruction. The second quality is that of simplicity, so that highly specialised and technical knowledge should not be essential in order to determine the ownership of a parcel of land. Thirdly, the system should be cheap, in order that the ownership of land should not be prohibitive to the small man on the grounds of cost of transfer; and, fourthly, the system should work reasonably quickly, so that a transfer of land should be effected with little more expenditure of time than is entailed in the transfer of other forms of property.

Systems of Land Transfer. To-day there are three separate systems of land transfer operating in this country. Firstly, the system of unregistered land, whereby proof of title is evidenced by a collection of deeds and documents generally retained in the custody of the owner

for the time being—deeds which a learned authority once remarked are "difficult to read, impossible to understand, and disgusting to touch." Each time a change of ownership occurs by sale, death or gift, a further document has to come into being to evidence the transaction.

The second system concerns the Deeds Registries of Yorkshire—a system two centuries old. Title to land in the greater part of this county is still evidenced by deeds and documents, but each change of ownership, each legal mortgage and a variety of other transactions have to be enrolled on the appropriate Riding register.

But it must never be forgotten that these registers are merely concerned with *documents* and not with *titles*, which still require to be substantiated by documentary evidence.

The third system is that of registered land, whereby documentary evidence is largely dispensed with, as the title to a parcel of land is found in an entry in the State Register of Titles. Let us test these three systems by the four characteristics mentioned just now.

As regards unregistered land, the element of security can hardly be said to predominate. Forgery and duplication of deeds by a fraudulently-minded owner of land are not unknown; there is the danger of essential documents being destroyed or defaced, with all the subsequent difficulty of getting duplicates, and on occasion it is hard to determine from old documents the exact boundaries to a piece of land. Owners of mortgages and other encumbrances who do not hold the documents of title have certainly been given some measure of security by the Land Charges Act, 1925, by the establishment of a public register on which their interests can be enrolled, but, as mentioned earlier,* this register is concerned not with land, but with the owners thereof; you file your claim against a name and not against a title. As the Chief Land Registrar has remarked, the value of the Land Charges Register is largely negative, in that the existence of a place

* See pp. 128 *et seq.*

where hostile interests can be recorded is a deterrent to a fraudulently-minded owner who might otherwise deal with the land to the detriment of other people. As regards the second element of simplicity, unregistered conveyancing is still highly involved, notwithstanding that the Law of Property Act, 1925, abolished a good many technical terms, and put trusts behind the curtain. There is still a welter of technical matter to master in perusing a title, an examination of dealings for 30 years back is required, the requisitions on title and the replies thereto have to be carefully considered, so that this system is still the province of the highly-trained legal mind.

Then the system is of necessity expensive, owing to the laborious investigation of title, notwithstanding that the period of deducing a title has been reduced from 40 to 30 years. If full scale fees are charged for a sale of land, they amount to a considerable item, on the first £1000, 1½ per cent on the purchase price being chargeable, plus 20 per cent of that 1½ per cent.

Lastly, unregistered conveyancing is certainly not quick —it is a slow game played according to time-honoured rules. There is a great gulf fixed between the decision to purchase a piece of land and the completion of the sale—the average time taken for completion being about two months.

As regards the Deeds Registries of Yorkshire, if we apply the foregoing tests, we find that an element of security is provided, inasmuch as the risk of duplication and forgery of deeds is minimised owing to their enrolment on a public register, a handy reference is provided should any deeds be lost, destroyed or defaced, and a useful history of the vicissitudes of ownership is kept on foot. Otherwise the system is just as insecure, just as complicated, just as costly and just as slow in its working as that pertaining to unregistered conveyancing.

It is in the system of registered titles that we see the four cardinal qualities of security, simplicity, cheapness

and quickness in full operation. The holder of an absolute title has the maximum of security in the shape of a State-guaranteed title. The documents employed are couched in simple terms intelligible to a layman. The system is considerably cheaper than that of unregistered conveyancing, the costs on either side, for example, on £1000, excluding out-of-pocket expenses, being less than half of those obtaining in the case of unregistered land. Furthermore, the registry fees have twice been reduced since compulsory registration was initiated.

Finally, the transfer of registered titles used to be expeditious and there was no room for the customary gibes about the methods of circumlocution of a Government department. For example, the average time taken in 1938 for first registration of title in London was 4·7 days—a remarkable record, in view of the detailed investigation required. Once a title was on the register it was possible to transfer the property in about three days. The advent of war in 1939 resulted in serious dislocation of the Land Registry routine and at the time of writing (1949) there is considerable delay in the completion of transactions with the Registry.

State registration of titles is largely in vogue in America and Europe and in some of the Colonies; in this country, however, it is compulsory only in the Administrative Counties of London and Middlesex and the County Boroughs of Eastbourne, Hastings, and Croydon; it is a voluntary matter in other parts of the country.

The initial attempt at registered titles is found in Lord Westbury's Act of 1862, which provided for a voluntary system of registration, but the expenses and complications of the system rendered it practically abortive.

The next attempt is found in the Land Transfer Act of 1875, still framed on a voluntary basis, but less complicated and restrictive than the original Act. It was the Land Transfer Act of 1897, however, which first put life into the dry bones by initiating a scheme of compulsory

registration. It provided for the system to be set in motion by Orders in Council following the petition of any county authority. The Act further provided that a county could be selected as the first compulsory area without the preliminary of any petition. London was chosen because the office of the Land Registry was already situated there and the large number of dealings taking place in land made it a suitable area in which to demonstrate the efficient working of the system.

Accordingly, commencing in 1899, the area was tackled parish by parish, and by 1902 the whole of the Administrative County of London was turned into a compulsory area. You must bear in mind, however, that not all land in London is on the register; the Act did not compel existing estate owners forthwith to register their titles—it only made registration compulsory when there was a disposition of land on sale or a grant of a lease for 40 years or more. Consequently, there are still some parcels of land in London which have not changed hands on sale since 1899, and therefore need not be put on the register unless the owners elect to do so.

The only authorities that have taken advantage of the statutory power to petition the Privy Council for an Order for compulsory registration are the County Boroughs of Eastbourne, Hastings, and Croydon, which became compulsory areas in 1926, 1929, and 1939 respectively.* Remember, however, that it is only in the cases of dispositions on sale and grants of leases of 40 years or more that land in these areas has to come on the register.

The Land Registration Act of 1925—part of what is known as the Birkenhead legislation—is the latest important enactment regarding registered land. Registration of title greatly appealed to the reformers responsible for the property statutes of 1925, and while the scheme was not adopted forthwith, the way was left

* The County of Surrey was to have been made a compulsory area in 1940, but the matter was postponed on account of the war.

open for the institution of compulsory registration, if after ten years' trial the reformed system of unregistered conveyancing did not work well. This was accomplished by Sections 120, 121 and 122 of the Land Registration Act, 1925, which provided that after 1935 Orders in Council might be made for compulsory registration without waiting for a petition from the county authority, and despite such body's veto. Safeguards are provided in the necessary approval of the Legislature of any draft order, and it is laid down that only one Order shall be made in the first year and only one county comprised in such Order.

The Land Transfer Committee appointed by the Lord Chancellor in 1934 recommended that Middlesex be the subject of the first Order. An order was consequently made whereby the County of Middlesex became a compulsory area as from 1st January, 1937.

Registrations in non-compulsory areas are more expensive from the Registry's point of view than compulsory registrations, although the fees are identical in both cases. Unmapped areas have to be surveyed and applications for voluntary registration are often prompted by the fact that the title is so complicated that sales are difficult and expensive to negotiate while the land is unregistered. Hence the slogan is sometimes heard: "If you have a bad title, register it." Incidentally, it may be noted that a voluntary title can be taken off the Register should an owner so desire, although such an occurrence is rare.

A pamphlet issued by the Land Registry says: "The keynote of the system of absolute title is that the machinery for the purchase and sale of land is assimilated to that of stocks and shares." There is an analogy between share registration and land registration which appeals to the layman, and possibly a study of the similarities of the two systems will give you some idea of the root principles of land registration. Thus, the title to shares in a joint stock company is an entry of the shareholder's name, address and description in the share register, together

with the distinctive numbers of his shares. The *prima facie* evidence of his title is a share certificate, which repeats these particulars, and a change of ownership of shares is accomplished by the completion of a form of transfer and its lodgment, usually with the share certificate, with the company's registrar, who cancels the old certificate and issues a new one in favour of the transferee. In like manner, the title to a parcel of registered land is found in an entry in the Land Register, of the name, address and description of the estate owner, together with the distinctive number of his title; the *prima facie* evidence of his title is a land certificate reproducing these particulars and a change of ownership of a registered title is made by the completion of a simple form of transfer and its lodgment at the Registry, together with the land certificate, which is either cancelled, and a new one issued to the transferee, or is suitably endorsed with the change of proprietorship.

Then Section 117 of the Companies Act, 1948, prohibits any notice of trust being entered in a share register—a company will not saddle itself with the safeguarding of trust interests. Similarly, Section 74 of the Land Registration Act, 1925, provides that, apart from settled land, the Land Registrar shall not be affected with notice of a trust, and references to trusts are, as far as possible, excluded from the register. It is of interest to note that this practice of excluding trusts from a title, first begun under the Act of 1897, has now been followed in the case of unregistered land, and trust interests are now "put behind the curtain."

Once again, a person interested in a holding of stocks and shares has a ready method of preventing the registered holder from dealing with them to his detriment by getting a "notice in lieu of distringas" served on the particular company or registrar, which obliges the latter to warn the interested party of any contemplated dealing in such shares. In the case of the Land Register, a person who has

a claim against or an interest in registered land is enabled to lodge a caution or other warning notice with the Registrar, the effect of which is to require the latter to give notice to the cautioner of any proposed dealings with the land. Lastly, if a share certificate is lost or destroyed a new one can be obtained on the giving of a satisfactory indemnity, in some cases accompanied by a statutory declaration. Likewise, if a land certificate is lost or destroyed the Registrar will issue a new one subject to the giving of an indemnity and advertisement in the *London Gazette* and elsewhere if deemed necessary. Two cases where the analogy breaks down may be noted, however. While the share register of a joint stock company is open to inspection by any member of the public on payment of a shilling fee, the Land Register is private, and can be inspected only on production of the written permission of the proprietor or on production of the land certificate. Lastly, while a joint stock company will often refuse to take notice of any lien or charge on its shares from outside parties, a section of the Land Register is reserved for recording any charges, liens or claims acquired by interested persons.

The Land Register. The Land Register consists of three parts. Firstly, the Property Register, which gives the title number, a short description of the property, such as the number in and name of the road, and a reference to the Land Registry General Map. Then there is the Proprietorship Register, giving the name, address, and description of the registered proprietor, the date when he was registered and usually the consideration money paid on the last transfer. It will also mention any fetters on the proprietor's full power of dealing with the title. Thirdly, there is the Charges Register, on which details of charges, leases and restrictive covenants, etc., are enrolled.

The land certificate, when issued, is a copy of the Land Register, having in addition a scale plan of the registered property. As it is possible, however, to enrol certain

items on the register without the production of the certificate, it means that the certificate does not always correspond with the register. The certificate, however, can always be sent to the Land Registry to be written up to date, and hence it is a simple matter to get the land certificate in line with the Land Register itself.

If many transactions take place over a short period with one registered title, it means that the register and certificate get overloaded with entries and thus you are approaching the state of affairs that exists when you have an unwieldy bundle of deeds relating to unregistered land. So the Registrar is empowered, if he thinks fit, to clear the register of cancelled entries and to issue a new certificate giving the existing position of the title.

The Law of Property Act of 1925 cut down the number of legal estates that could exist in land to two, and so we find that the only titles now capable of registration are freeholds and leaseholds. All freeholds in a compulsory area must be registered and so must all leaseholds with more than 40 years to run. Leases with less than 40 years, but more than 21 years to run, can be registered at the option of the leaseholder, with the exception that, where the freehold interest out of which the lease is carved is registered, any lease with over 21 years to run must be registered, whether in a compulsory or voluntary area. Leases with less than 21 years to run cannot be registered, neither can a lease containing an absolute prohibition against alienation nor a lease for a mortgage term. By Section 74 of the Land Registration Act, 1925, trusts are as far as possible kept off the title, and the Registrar is not concerned with the fiduciary capacity of registered proprietors. Trust interests, however, find a place in the proprietorship section of the register in some cases; thus, in the case of a tenant for life (who will have the fee simple vested in him), a restriction will be entered in the proprietorship section whereby no transfer on sale will be registered unless the consideration money is paid to the

trustees of the settlement or into Court. Then there is the more familiar instance of property in joint names—where A and B are deemed to hold the property as trustees for themselves. In such a case, a note will be made in the proprietorship section of the register to the effect that no transfer on sale will be registered unless the capital money is paid to at least two trustees or to a trust corporation.

There are all sorts of interests that can be protected by registration on the register—interests which in the case of unregistered land would be registrable in the Land Charges Register. Thus deeds of arrangement, receiving orders and pending actions are protected by lodging a creditor's notice, an inhibition, or a caution respectively. Then restrictive covenants and annuity charges may also be entered in the charges section.

Personal covenants are not entered in the charges register, for they do not affect the title to a parcel of land. In certain cases, however, they are kept in evidence by stitching in the land certificate on first registration an office copy of the conveyance or grant of a lease, etc., wherein such personal covenants are recited. If after a title has been registered, a transfer thereof containing personal covenants is registered, an office copy of such transfer may also in certain cases be stitched in the land certificate. Then there are certain rights affecting land which are not found in the abstract of title if you are dealing with unregistered conveyancing, but have to be inquired about elsewhere. Thus *easements*—right of way and drainage, etc.—will be found by inspection of the land; leases of not more than 21 years at a rental will be disclosed by inquiry of the occupier; rights under the Public Health Acts and the various Building Acts will be revealed by inquiry of the particular local authority. All these matters, if affecting registered land, will have to be checked in like manner, and attention is drawn to them on the inside cover of up-to-date editions of land certificates.

When you are dealing with registered land you will usually be concerned with one of three classes of title—absolute, good leasehold and possessory; there is a fourth—and practically unknown class—a qualified title, granted where the title can only be vouched for over a limited period or subject to certain reservations.

An Absolute Title gives the proprietor a good title against all the world, a title guaranteed by the State, and once it is granted, the land certificate is the only essential document to prove ownership of the land, and the former evidence of title in the shape of title deeds is redundant from the point of view of proof of ownership. It will occur to you, however, that it may be dangerous to have two lots of documentary evidence existing relating to one parcel of land—the title deeds and the land certificate. The answer to this is that on first registration the Land Registry stamp is branded on each and every document relating to the title, and the presence of this stamp is a warning to any party contemplating a purchase or a mortgage of the land, that a land certificate is in existence.

Then there is Good Leasehold Title, devised to meet the needs of leaseholders who, while giving satisfactory evidence of their leasehold title, cannot, as is usually the case, produce proof of the freeholder's title to grant the lease. It is an anomaly of the law of property that the purchaser of a lease is not entitled to call for proof that the original lessor was the rightful owner of the freehold, and the validity of the original lease is always assumed in transactions with leasehold property. In cases where the freeholder's title is vouched for—as where it is registered with an absolute title—the leasehold may be registered with an absolute title. It is possible to get a good leasehold title converted into an absolute one after 10 years, on proof that the proprietor or successive proprietors have been in possession for that time.

With a good leasehold title, you want something more than the land certificate as your title deed—the original

lease must accompany it—although in practice all intermediate deeds are generally found.

The third type of title—Possessory—has defeated the essential notion of registration of title because it is a mixture of the old system and the new. On application for first registration of a possessory title, the Registrar satisfies himself only that the present owner has a *prima facie* right to the property. He does not ensure that there is a good chain of title for the past thirty years, but all dealings subsequent to registration have to be effected by registered instruments. Thus all deeds prior to registration should accompany the land certificate, and on each change of ownership the title up to the time of registration has to be investigated in the old-fashioned way. After the inception of compulsory registration in 1897, a possessory title was the most popular—it was the only compulsory title in a compulsory area, and smaller fees were payable on first registration. The first step to remedy this state of affairs was the provision of a common scale of fees for all titles, and the second and more drastic step was taken in the Act of 1925, which took the option out of the applicant's hands and gave the Registrar discretion to refuse a possessory title and to grant an absolute or good leasehold title, whether the applicant is amenable or not.

As a result, in 1938 only 1 per cent of first registrations were given possessory titles.

Existing possessory titles can be turned into absolute or good leasehold ones if fifteen or ten years old respectively, and in one year over 5500 cases were so treated.

I make no apology for this long digression on the history and idea of registered land, for, while the aid of our friend the branch solicitor still has to be invoked in most cases when handling registered titles as security, the system is sufficiently devoid of technicalities to make it intelligible and interesting to a layman, whereas a capable grasp of unregistered conveyancing is only possible to the legal and specialised mind.

We now come to the precautions and formalities to be observed in taking registered land as security. I mentioned earlier that when dealing with registered titles you speak a different language, you are in another country as regards mortgages and their attendant formalities; legal mortgages become registered charges, title deeds give place for the most part to land certificates. The type of charge taken, the registration effected and the searches made are all in a category different from that appertaining to unregistered land.

Legal Charge Over Registered Land. We will consider first of all the procedure to be adopted when it is proposed to take a legal charge over registered land offered as security. You will recollect that in the case of unregistered land a legal mortgage is got by a grant of a long term of years in the property, if freehold, or a sub-lease if leasehold, with an alternative method of taking a charge by way of legal mortgage in either case. With registered land you get your legal estate by means of a registered charge, which by the Land Registration Act, 1925, puts you in the same position as if you had got a lease of 3000 years, if you are concerned with a freehold, or a sub-lease for the term of the lease less one day, if a leasehold. You, furthermore, are endowed as chargee with all the powers and remedies of a legal mortgagee. First of all, you should make sure that you have got all the essential documents of title. If you are dealing with a freehold absolute title, nothing beyond the land certificate is normally required. If the land is registered with a good leasehold title you will require the land certificate and the original lease, although you usually find any intermediate documents present. If you are dealing with a possessory title, however, you will want not only the land certificate but also all the documents of title up to the date of first registration, and this will usually entail a professional examination of title as in the case of unregistered land. Then you will identify the land concerned by reference to the property

section of the land certificate which gives you a short description of the property and an extract from the Land Registry map. Sometimes you may find that the description in the land certificate does not tally with the description given by the borrower—he may be offering you a dwelling house as security, while the land certificate shows a vacant plot of land. An investigation on the spot will, of course, satisfy you as to what your security actually comprises, and the register and the land certificate can be suitably amended by the Registrar. You should also peruse the proprietorship sections of the certificate to make sure you are dealing with the person registered as proprietor. The consideration money that passed when the borrower bought the property will usually be found here, and this is a useful check on—but not a basis for—the value you are going to place on the land for lending purposes.

The next preliminary step is to ascertain that there are no charges outstanding in front of you and no encumbrances such as detrimental restrictive covenants, writs, etc. This can be done by searching the Land Register, either personally or by post.

Personal searches, costing one shilling, are discouraged by the Registrar for they are neither desirable nor necessary, in view of the ample facilities provided by way of an official search. The virtues of the latter are that any errors are the responsibility of the Registry, whereas if anything is missed in a personal search, so much the worse for the searcher.

An official certificate of search is got by the completion by your solicitor of Form 94 (Application for Official Search) in duplicate, which is forwarded by post to the Registry, accompanied by the written authority of the proprietor of the registered title or his solicitor. The duplicate search form (94A) will be returned by the Registry free of charge to an intending chargee, with office copies of any adverse entries appearing on the Register.

Assuming that the search reveals a clear Charges Register, an application for registration of your charge should be lodged with the search certificate within fourteen days of the date thereof. No adverse entries that have been made between such date and the date of application for registration will then affect you, unless such entries relate to a mortgage caution (see page 177) or to a priority notice. A party proposing to take a charge over registered land may give a priority notice on Form 18, accompanied by the land certificate. If the charge is delivered for registration within 14 days of the giving of the notice it will take priority over any application or instrument that may have been delivered in the meantime.

In case of urgency a search may be requested by telegram or telephone in accordance with Rule 293 of the Statutory Rules and Orders, but the reply will be limited to a statement that there is no subsisting entry or otherwise.

Land in Yorkshire with a registered title is clean outside the provisions of the respective Deeds Registries, and search is necessary at the Land Registry only. The Land Charges Act, 1925, provides that land charges, pending actions, writs, orders, etc., affecting registered land which can be protected by the lodgment of inhibitions, cautions, creditors' notices, etc., shall not require registration on the Land Charges Register, so you will not need to search there, but on the Land Register of Titles. It is true that the Registrar is under no duty to ascertain if an application to register a charge on the Land Charges Register refers to registered land, and if any such charge is registered thereon it will not affect an interested party who searches the Land Register, for it is registered in the wrong place.

As regards any bankruptcy disability under which the borrower may be labouring, it is necessary to point out that all petitions in bankruptcy are, in the first instance,

lodged at the Bankruptcy Office, and a daily list of such petitions is furnished to the Land Registrar, who registers them all as pending actions in the first section of the Land Charges Register. As soon as possible thereafter the index of names of proprietors of registered titles in the Land Register is searched, and if the insolvent party's name is found thereon the Registrar transfers the entry to the Land Register as a creditors' notice. Notwithstanding the preliminary entry on the Land Charges Register, there is no need as regards registered land to search elsewhere than on the Land Register—Section 61 (2) of the Land Registration Act, 1925, makes this clear.

If circumstances make it expedient—such as where you are dealing with a building estate or with a new property—the registers of the local authorities should be searched for any charges or restrictions put on by them.

Execution of Charge. Assuming that all the necessary searches have been made, the next step is to get your charge executed and registered. A charge on registered land need not be in any set form—it must be by deed, but may be in any form, provided that the land which is charged is identified by reference to the title number on the register, or in any other manner sufficiently precise without reference to other documents, and that the charge does not refer to any prior and unregistered interest. The Land Registry supply a form of charge (Form 45), but banks use their own forms, which are drawn to cover all contingencies. For example, the bank form expresses the charge to cover all moneys owing now or hereafter, to save the rule in *Clayton's* case operating detrimentally. The borrower covenants to repay the advance on demand and to keep the property insured; his statutory power of leasing is made subject to the bank's consent and the right of consolidation is expressly reserved to the bank.

The charge, having been duly executed, will require stamping as a mortgage by deed at the rate of five

shillings per cent on the amount it is proposed to lend, if no limit is expressed in it, otherwise the duty will be calculated on the named limit. In this connection, the Registrar now undertakes to get the necessary Inland Revenue stamps affixed on documents sent for registration and does not charge for this service.

Registration of Charge. The final step is registration of the charge at the Land Registry, and the following procedure must be adopted. The charge, together, with a copy thereof, must be lodged at the Registry, preferably by post, with the relative land certificate and search certificate. The duplicate charge and the land certificate will be retained there and a charge certificate will be issued to you within which will be stitched the original copy of the charge. This charge certificate will represent your security. The fee for registration of a charge is 4s. per cent up to £750, with a sliding scale for higher figures.

Before 1926 the land certificate was not impounded by the Registry, which explains why you sometimes find both this document and the charge certificate in your possession. When it first became the practice to retain the land certificate at the Registry, a green receipt was given for it, but since the Land Registry rules of 1930 came into force no receipt is issued.

If your security was taken before 1914, you may not have a charge certificate in full form, but merely the land certificate and an office copy of the charge, upon which is endorsed a certificate of registration.

The priority of registered charges is of necessity regulated by considerations differing from those which obtain in the case of unregistered land—where, you will recollect, possession of the title deeds is the determinant factor. With a legal mortgage of registered land, priority depends on the date of registration of the charge, not on the date of its creation. By Section 30 of the Land Registration Act, 1925, where a charge is drawn to secure further advances as in the case of a bank charge, the Registrar must advise

the chargee before making any entry in the register—such as a second charge—which would adversely affect the priority of any further advance by the first chargee. If an advance is transferred to another branch, it is desirable to advise the Registrar of the change of address, for while any loss in relation to a further advance, occasioned by delay in the post, will be made good by the Registry, losses arising from failure to amend the address for service will be suffered by you.

It is of interest to contrast the effect of registration of a second charge on registered land with the effect of registration on the Land Charges Register of a second mortgage on unregistered land. In the latter case, unless direct notice is given to the banker and providing he does not search the register, further advances by him are not subject to the second charge; but in the case of registered land, a banker having taken a charge to secure further advances will, as mentioned just now, be advised by the Registrar of the intended registration of a second charge, and hence must break the borrower's account to preserve priority and to avoid the rule in *Clayton's* case operating to his detriment.

The only exception would be where, by the terms of the charge, the banker was under an obligation to make further advances and such obligation was noted on the register. This is provided for in the Law of Property Amendment Act, 1926, Section 5, which brings registered land into line with unregistered land as regards tacking The cases, I imagine, however, are rare, where a banker is under a binding covenant in his charge to advance a specific sum.

Mortgage Caution. Section 106 of the Land Registration Act, 1925, prescribes an alternative method of taking a legal charge over registered land—namely, by the execution of an ordinary legal mortgage, as in the case of unregistered land, and the registration of a special form of caution at the Registry. This must be accompanied by

the land certificate, the mortgage deed and a certified copy thereof. The caution is entered on the Proprietorship Register and the certified copy of the mortgage is filed, the original instrument being returned to the mortgagee. I understand, however, that this method is practically unknown.

Equitable Mortgages. Now for the question of equitable mortgage of registered titles. This is accomplished by the simple deposit of the land certificate with the lender, such deposit creating a lien equivalent to a lien created by the deposit of title deeds of unregistered land. The Act provides statutory protection for such a charge in that, if notice is given to the Registrar of the deposit of the certificate, he will advise you of any proposed dealings with the land.

This notice of deposit should preferably be given in duplicate on Form 85 A, and a registration fee of one shilling is chargeable. It should be signed by the branch manager or acting manager, and "per pro" signatures are not accepted. Before the war, the duplicate notice of deposit duly endorsed by the Registry was returned promptly, but the exigencies of war-time still persist at the Land Registry and the notice of deposit of the land certificate is now merely acknowledged by a postcard. Such acknowledgment gives the same priority as from the date of the postmark as would have been given if a duplicate notice of deposit had been received back duly receipted by the Registrar. This postcard acknowledgment is no guarantee however that no prior notices of charge have been received. I want to make it quite clear that, as far as the Registrar is concerned, your security is found in the deposit of the certificate and the filing with him of the notice of its deposit—he is not aware of, and not concerned at this stage with, any form of charge you may take.

As in the case of a legal charge, you should therefore make sure that no prior charges or encumbrances exist before you lend any money on the strength of your

equitable charge. The simplest and most efficacious way, however used to be to forward your notice of deposit together with the land certificate to the Registry, who would enter the latter up to date, to include your notice of deposit. On the return of the certificate it was a simple matter to see if there was anything entered thereon detrimental to your interests. Sometimes borrowers or their solicitors objected to the notice of deposit being entered on the certificate, and as it is not essential for your security that this should be done, there was no harm in indulging them. In such a case any subsequent cancellation of the entry in the register would not involve mention of it on the certificate.

The speediest method in these post-war days is to have a postal search made on Form 94 as in the case of a registered charge. But no breathing space of fourteen days is given as when you are taking a registered charge. A depositee of a land certificate is not a purchaser or mortgagee within the meaning of the Land Registration Rules and therefore cannot obtain priority for registration of notice of the deposit of the certificate.

I think you will find that where a bank is content with an equitable charge by deposit of the land certificate, it does, in fact, get the borrower's signature to a form of charge under seal, which is duly stamped but not registered. The reason for this sort of half-way house is that the form provides, as we have seen, for all sorts of stipulations in favour of the banker; it puts powers and remedies in his hands which can be exercised without recourse to the Court, as would have to happen if he relied on the simple deposit of the certificate. If at any time you wish to perfect your security, it is a simple matter to turn your equitable interest into a legal estate by registering your charge. You must be careful, however, to get your charge by deed—a charge under hand could not be registered at a later date. It may be asked—why not go all the way in the first instance and

register your charge? The answer is, of course, that registration involves a fee, round about four shillings per cent, and that in some instances borrowers, in the case of temporary advances, prefer the charge to be kept off the title.

You sometimes get a complication where you have given notice of deposit of the land certificate, keeping your charge in the background, and the borrower gives a second charge to another party, who attempts to register his charge. In accordance with the rules, you will immediately be advised by the Registrar of the intended registration, and if you do not take action within 14 days the notice of deposit will be removed from the register. Usually, the second charge will refer specifically to your charge, and in such a case the Registrar will require you to register it forthwith, if by deed.

Sometimes you propose to lend money against an equitable charge of a registered title where the lender has not got a land certificate in his possession, either because the title is in process of registration for the first time or a transfer of an existing title to him is not yet completed. The Land Registry rules provide in such a case that notice of intended deposit can be lodged at the Registry, in which case the land certificate, when ready, will be issued to the lender named in the notice. Notice of intended deposit operates as a caution in the same way as notice of deposit, but it will require signing by the borrower as proprietor of the registered title. When the land certificate comes to hand there will be no necessity to give notice of deposit; the original notice of intended deposit still stands.

You may sometimes be under the necessity of taking a second mortgage of a registered title; this is done by lodging your charge in duplicate at the Registry and getting a certificate of second charge. Alternatively, you can get your second charge duly executed, but not register it, protecting yourself by lodging a caution at the Registry.

You should give notice of your charge to the first chargee and ascertain from him or from the register if he is bound to make further advances.

Then occasionally you may be offered a sub-mortgage of a registered title. That is to say, your customer has lent money on a registered charge and offers you this charge as security—that is, he gives you a sub-charge. There are two methods of effecting this: you can lodge the charge certificate at the Registry, together with your sub-charge, in exchange for which you will be given a certificate of sub-charge as your security. Alternatively, you can get an equitable sub-charge by giving notice of deposit of the charge certificate to the Registry, and then your security will be the charge certificate, plus the Registrar's acknowledgment of your notice. In such a case you will usually get a sub-charge executed by your customer, although you do not register it.

Repayment of Advance. Two other matters remain for our consideration—the procedure to be adopted when an advance is paid off, and the steps to be taken if circumstances demand the realisation of your security. If an advance is repaid and the security is vacated, the routine to be followed depends, of course, on whether you hold a registered charge or an equitable charge by deposit of the land certificate. In the first case, you will complete and forward to the Land Registry Form 53 (Discharge of Registered Charge), together with the charge certificate. Provided that the form of discharge does not have any sort of reconveyance added to it, a twopenny stamp will suffice; otherwise, stamp duty at the rate of 6d. per cent on the highest amount advanced on the strength of the charge will be required. The seal of the bank will be required to the form of discharge.

If the borrower has sold the property forming your security, you will generally find Form 55 used, which is a combined form of transfer from your customer to a

purchaser, plus a discharge on the bank's part. No fee is payable for a discharge of a registered charge. Where your security has consisted of the deposit of the land certificate, plus notice of its deposit to the Registry, all that is necessary to free the land from your charge is to forward to the Registry an application to withdraw the notice of deposit—usually the form found on the back of the Registrar's acknowledgment of your notice of deposit is used. The land certificate must accompany the application, which does not require sealing, but merely the official signature of the branch manager or his deputy, who must not sign "per pro" however. No fee is payable, and the land certificate will be returned with the notice of deposit deleted from the charges section if it was entered in the first instance.

If a part only of the land subject to your notice of deposit is being released, a letter to the Registrar withdrawing your charge over the specified plot is all that is necessary, and the land certificate, duly amended, will be returned to you. These partial releases usually occur where a building estate with a registered title is charged to a bank, and, as each house is sold, the purchaser is given a registered title and a land certificate.

The most efficacious method of procedure if you have been content with an equitable charge is, on the first sale, to send in letter form a signed notice of withdrawal of your charge over the particular plot, together with the land certificate, which the Registrar is requested to retain for the time being. On completion of each subsequent sale, all that is necessary is a note to the Registrar, who will eventually return the land certificate to you if any land is still left on the original title.

In connection with land certificates relating to building estates, the Chief Land Registrar asks me to state that if you find the property register burdensome and difficult to read owing to a long list of removals of part of the

title, it is only necessary to forward the certificate to the Registry and a new and up-to-date edition will be issued free of charge.

You will recollect that I mentioned the practice of banks to get a form of charge executed by a borrower, even where it is not proposed to register it, but merely to rely on notice of deposit of the certificate. In such cases, where the security is being vacated, most solicitors are content with the cancellation of the charge form and the withdrawal of the notice of deposit. But in some cases they press for a statutory receipt to be sealed on the back of the form, and this is usually done as a matter of courtesy and expediency.

Realisation. Now for the melancholy cases where the bank is under the regrettable necessity of exercising its power of sale over the security. If you have a registered charge, and the borrower is in default, you are armed forthwith with all the powers and remedies given by the Law of Property Act to a legal mortgagee and can appoint a receiver, enter into possession, foreclose, or sell, as you think fit. The considerations likely to influence you are, of course, those I mentioned in connection with unregistered land.*

If you are successful in selling the property, you can give a good title by completing Form 31, which is the standard form of transfer on sale provided by the Registry, duly amended to cover the case of sale by a chargee. Where you have only got an equitable charge by deposit of the certificate, you are in precisely the same boat as any equitable mortgagee who has not got a charge under seal—your only recourse and remedy is to apply to the Court for an order for sale. But if you have taken the precaution to get a form of charge executed under seal, in addition to getting the deposit of the certificate duly protected by notice of deposit, you are in a far better case; for it is only necessary to turn your equitable interest

* See p. 151 *et seq.*

in the security into a legal interest by registering your charge, and you can then proceed as expediency dictates, armed with all the rights and remedies of a legal chargee. This, possibly, is the main reason why banks usually get a deed of charge signed when the land certificate is deposited as an equitable security, even though they never contemplate registering it while things are normal.

In all cases where a power of sale is exercised, it is necessary before paying over any surplus proceeds to the borrower, to make sure that there are no parties better entitled than he to such moneys, such as a second chargee, and this will not usually mean searching the Register, for if your charge is drawn to cover further advances the Registrar will have notified you of any registration of a further charge.

You may recollect that charges given in respect to such matters as land improvement and drainage schemes are registered, if relating to unregistered land, as Class A or B land charges on the Land Charges Register, and that once registered they have priority not only over future charges of any kind but also over existing charges.* In the case of a similar charge acquired over registered land, however, it is necessary, if priority is claimed over earlier charges, for a written claim to accompany the registration unless it is incorporated in the charge itself. The Register will then be endorsed that priority is claimed under the particular Statute referred to, and that the charge does not rank for priority, as regards earlier charges, according to the date of its creation or registration.

Companies. There are one or two points concerning limited companies as borrowers against registered land that deserve to be noticed. Firstly, the fact that you register your charge on the Land Registry, or give notice of deposit of the land certificate, does not dispense with the need for registration at Bush House in accordance

* See p. 132 *et seq.*

with the provisions of Section 95 of the Companies Act, 1948. This should be effected before any registration is applied for at the Land Registry, for by Rule 145 the certificate of registration issued by the Registrar of Companies is required to be produced to the Land Registrar, otherwise he will mark the Register that the charge is subject to the provisions of Section 95 of the Companies Act.

Also, searches will not only have to be made at the Land Registry but also at Bush House, in the usual way, not forgetting any local searches that may be expedient.

In the case of a sale by the company, if no registered charge has been taken, but merely notice of deposit of the certificate given, it is probable that the bank will be required to join in a transfer and discharge on Form 55, for although the Registry will accept a withdrawal of the notice of deposit or a written release of part of the title concerned therein, a purchaser's solicitor will be aware of the existence of a written charge, owing to its registration at Bush House.

If you take a debenture which includes a specific charge on registered land, then the debenture can be registered as a charge. A certified copy of the debenture must be lodged at the Registry, together with the relative land certificate, and the original debenture will be sewn up in the charge certificate.

Alternatively, if there is a trust deed containing a specific charge, the trust deed can be registered as a charge. It must be accompanied by two certified copies, one of which will be filed at the Registry and the other stitched in the charge certificate. It must also be accompanied by the land certificate. If preferred, the trust deed itself can be incorporated with the charge certificate, and then only one copy need accompany the application. If a simple and specific charge referring to the trust deed or debentures is taken, a certified copy for filing of the trust deed or debenture must accompany the copy of the charge.

A floating charge cannot be registered on the Land Register, but can be protected by a notice under Section 49, provided that the land certificate is produced. If you do not get the land certificate with your floating charge, you can protect yourself by lodging a caution under Section 54 of the Land Registration Act, 1925.

Legal Mortgage of Equitable Interest. Occasionally you are asked to lend money against a legal mortgage of an equitable interest in land. For example, a beneficiary under a trust for sale may wish to borrow on his interest, a joint tenant may offer as security his interest in property jointly held, a remainder-man may want to raise funds on his reversionary interest in an estate.

In all these three cases, the would-be borrowers have only equitable interests to offer—they cannot charge any legal estate. The beneficiary under the trust for sale has his rights solely against the proceeds of sale of the corpus of the estate in the trustees' hands; the joint tenant can only charge his share of the proceeds of sale of the joint property. He may hold the legal estate jointly with his co-tenant as trustee, but it is not as trustee that he wants to borrow, but as beneficiary under the trust. The owner of a reversionary right likewise has no legal estate to offer, but simply his equitable interest. Now, in all such cases, the mortgage you take will not be accompanied by title deeds, for it is a mortgage of personalty, not realty. Occasionally you do get the deeds, but that is usually because the trustees do not know their job.

You will recall that mortgages of unregistered land unsupported by the relative title deeds can be protected by registration on the Land Charges Register, but mortgages of equitable interests cannot be similarly protected by registration as land charges, for they are not charges on land but on personal property. To avoid the consequences of the trustees of the estate concerned selling and distributing the proceeds of sales to the beneficiaries, in ignorance of the mortgage, it is now provided

that written notice of the charge can be given to the trustees, or a trust corporation appointed for that purpose, thus warning them against paying out the proceeds of sale regardless of the lender's interest.

You will, of course, be careful to get an acknowledgment from the trustees of your notice and file it with your mortgage. You should likewise make sure by inquiry that the trustees have not received any prior notices of mortgage from other parties. Should there be more than one mortgage of the same equitable interest, priority is determined by date order of receipt of the respective notices by the trustees.

In the case of a mortgage by a joint tenant, alternative protection can be gained by getting a memorandum endorsed on the holding deed, giving notice of the lender's interest in the proceeds of sale.

If the equitable interest which is being charged issues out of registered land, a mortgage thereon can be protected by registration on a register set up under the Land Registration Act, 1925, termed the "Minor Interests Index." Priority among competing charges on the same equitable interest is settled by date order of registration on the minor interests index. You must not forget, however, that this index is not part of the land register, and does not affect a purchaser or chargee of the legal estate.

Where stocks and shares are concerned, a notice in lieu of distringas (see p. 213) is sometimes served on the respective registrars as a protective measure.

A warning may not be out of place here concerning advances against reversionary interests—make sure that the reversion against which your customer wishes to borrow is absolute and not conditional. That is to say, ascertain if the benefit of the reversion passes to your customer's estate, if he predeceases the life tenant, or *if the reversion is contingent on your customer surviving* the life tenant. If the latter is the case you will require your security to be supported by a life policy to cover

the borrower's untimely death. The drawback of a reversionary interest as security is that you cannot foreclose on the assets of the estate to which it relates—you can only sell the reversionary interest to another party.

CHAPTER VII

STOCK EXCHANGE SECURITIES

"Dead loans are sometimes produced by lending money to parties to buy shares in public companies. There was too much business of this kind transacted by some bankers a few years ago. The party did not at first, perchance, apply to his banker to enable him to purchase the shares; but the calls were heavy, and his ready money was gone; he felt assured, however, that in a short time he should be able to sell his shares at a high profit; he persuaded his banker to pay the calls, taking the shares as security. Other calls were made, which the banker had to pay. The market fell; and the shares, if sold, would not pay the banker's advances. The sale, too, would have caused an enormous loss to the customer. The advances became a dead loan, and the banker had to wait till a favourable opportunity occurred for realising his security."—*The Logic of Banking*, by J. W. Gilbart.

STOCK Exchange securities have much to recommend them as cover for advances, for the perfection of the security involves little formality and is accomplished at comparatively small cost; likewise the release of the security can be effected with a minimum of cost and formality; there is no elaborate investigation of title required, and the cardinal virtue of ready realisability is present. Possibly, however, what was formerly looked upon as a favourable element is no longer present—that is, stability of value. The experience of the past few years has shown that margins of cover are likely to run off with disturbing suddenness, and not even the gilt-edged variety has been immune from a drastic fall in price, necessitating calling for additional cover. Now, what has happened once may conceivably happen again, and thus it is expedient to keep a vigilant eye on all advances against stocks and shares where a bare margin of security exists.

We will plot out our consideration of the subject into the

three categories of "bearer," inscribed" and "registered" securities.

Bearer Securities. Bearer securities consist of that class of security the title to which passes by mere delivery of the instrument, such as bearer bonds, debentures payable to bearer, stock certificates to bearer, share warrants to bearer and certain types of certificates mainly of American origin, which are endorsed in blank by the registered holder.

In all but the last case these instruments are recognised by the Courts as fully negotiable. You will no doubt recall that a negotiable instrument must respond to three tests: the property in it—that is, the legal ownership—must pass from hand to hand by mere delivery, or, in the case of instruments payable to order, by endorsement and delivery; secondly, a party who takes it honestly, for value and without notice of any defective title in the transferor, acquires an indefeasible title against all comers; and, thirdly, it must contain a right of action in itself—the holder must be able to sue in his own name. The last type I mentioned—the certificate endorsed in blank—is not fully negotiable, because it does not respond to the last test—the holder is unable to sue in his own name unless and until he has the security registered in his name.

You will readily see that the bearer type of security is an ideal form of cover from the point of view of title, for, provided you act in good faith—that means honestly—and give value—that is involved in advancing money against the security—and have no actual notice of any defect in the borrower's title, you can hold the security against all the world.

And remember that it is not a question of what you *ought* to have known; provided you do not shut your eyes to the facts in front of you, constructive notice does not enter into the matter. In the case of *London Joint Stock Bank* v. *Simmons*, [1892] A.C. 201, where a stock-broker pledged bearer bonds belonging to his clients, the House of Lords upheld the bank's right to hold the

bonds against its advance, and Lord Herschell said: "I should be very sorry to see the doctrine of constructive notice introduced into the law of negotiable instruments." In other words, provided facts are not present, the neglect of which would amount to bad faith, you are not bound to probe into the question of the borrower's title.

The Exchange Control Act, 1947 provides that bearer securities must be lodged with or to the order of an approved bank chosen by the owner of the security. This control was imposed to prevent the transfer of British-owned securities to foreign ownership except for value received. The ownership of such bearer securities will not be affected by this regulation, but the depositee bank will be under a duty to ensure that no illegal transfer of such items is made.

Bearer securities are taken as cover by way of pledge, and it is perhaps timely to remind you of the essential differences between pledge, mortgage and lien. A pledge arises where chattels or negotiable instruments are deposited with a party as security for money lent. The essence of a pledge is that possession passes to the pledgee, while the property in the thing pledged—that is, the legal ownership—remains with the pledgor. Sometimes, of course, possession of the thing itself does not pass, but merely the documents of title, as in the case of merchandise advances under the provisions of the Factors Act, 1889.

In the case of a mortgage, other than that of land, the property in the thing mortgaged—the legal ownership—passes to the mortgagee, while possession of it may or may not remain with the mortgagor. Lien is a right of retainer over property exercisable in respect of a debt and arises by implication and not by specific charge or agreement. It can only be exercised where there is no expressed or implied contract inconsistent with it. Where, for example, there is an explicit contract of bailment—to hold articles for safe custody—there can be no lien. A banker's lien was described by Lord Campbell in the case of *Brandao* v. *Barnett* (1846), 1 M. & G. 909, as "a general

lien on all securities deposited with them as bankers unless there be an express contract or circumstances that show an implied contract inconsistent with lien."

Bearer bonds may conceivably be the subject of a lien if they are not essentially lodged for safe custody or to support an advance. If they come into your hands as cover, however, you have a pledge, and not a lien.

The mere deposit of bonds with intent to pledge will give you all the rights of a pledgee, but it is usual to take a memorandum of deposit under hand specifying the terms of their lodgment, and usually giving a power of sale on default.

When taking bearer bonds as security, you should, of course, see that they are in such a state as will make them good delivery if realisation becomes necessary; thus the Revenue stamp should be in order, all unpaid coupons should be present and no marking of any kind in ink should be made. It will be your duty to watch for any drawings of such bonds.

Then there is the kind of certificate, first in use by American railways, but now largely favoured by American and Canadian business corporations, which once endorsed passes from hand to hand by delivery, and thus acquires one of the characteristics of a bearer bond. The name of the registered holder is set forth on the front of the certificate and on the back is a form of transfer combined with a power of attorney. The registered holder signs the form of transfer under proper attestation, and thenceforward the certificate is transferred like a bearer bond, except in cases where the transfer has to be by deed. When such a certificate is offered as security, you may find that it is in a good marking name, that is, in the name of London stockbrokers or a trust company, who specialise in such business, and, being properly endorsed, you may safely regard it as a bearer bond. If it is in the borrower's name, however, you must remember that even when duly endorsed by him he is still the registered holder and

there is the possibility, remote though it may be, that the shares are subject to a lien by the issuing company or to some prior charge or interest.

The precaution of getting such certificates registered in the name of your nominee company is cumbersome, for in 1931 the Committee of the London Stock Exchange decreed that, with one exception, shares of this description in the names of limited liability companies, corporations, societies or institutions constitute bad delivery unless each certificate is stamped with the signed guarantee of such holder that all necessary papers have been filed with the Registrar and/or transfer agent to ensure that no hitch will occur if a transfer is put forward for registration. Short of this formality or of putting such certificates in the name of a personal nominee, they can only be left in the name of the borrower. If, of course, they are not in his name or in a good market name, they should be registered in the borrower's name and endorsed before being used for security purposes. When getting this type of certificate endorsed it is important to see that the holder's full signature is given, including any courtesy title, if an American certificate.

This type of security requires stamping at the rate of threepence for every £25, and every fractional part of £25 of its nominal value when first assigned, transferred or in any manner negotiated in the United Kingdom (Finance Act, 1899). Certificates of no par value do not require stamping. By Rule 136 of the Stock Exchange a member cannot be required to accept delivery of a certificate of American shares representing a larger number than 100 of $5 each, with a sliding scale for larger denominations. This should be borne in mind when taking such shares as security.

Inscribed Stocks.* As you are aware, the title to inscribed

* As from 1st January, 1943, inscribed stock for British Government securities was abolished and all such holdings are now treated as registered stock. Other inscribed stocks domiciled at the Bank of England have been similarly treated.

stocks is comprised solely in an entry of the stockholder's name in the books of the Registrar, and no indicia of title are available, the stock receipt being merely a memorandum of the inscription. As the stock can be dealt with without production of such receipt, no reliance should ever be placed on such a document for lending purposes, or, for that matter, as evidence of means. The one sure and effective method of getting inscribed stocks as security is to have them inscribed in the name of the bank or its nominee, usually a company specially incorporated for such purposes. In such a case you get a legal mortgage of the stock—the legal ownership is vested in you, subject, of course, to the borrower's right of redemption. It is customary to take a standard memorandum of deposit which puts beyond dispute the purpose for which the stock was transferred, and sets forth the conditions under which the bank may sell.

There is an alternative and little-known method of getting some sort of security over inscribed stocks without the formality of transfer into the lender's name—by the execution of a charge wherein the borrower covenants not to deal with the stock without the bank's consent. Sometimes a power of attorney is added, empowering the bank or its nominee to sell. Such a charge would undoubtedly give you an effective equitable mortgage. Clearly this is not a method to pursue, except in the case of temporary borrowings by an absolutely undoubted customer, and an instance I can call to mind is the case of an incorporated charitable society holding large blocks of all sorts of inscribed stocks, which required accommodation for six months only.

Occasionally, the title to certain stocks of the Canadian and Australian Governments, officially designated inscribed stocks, is evidenced by stock certificates which must be produced on sale or transfer. These must be regarded as being in the category of registered stocks.

Registered Stocks and Shares. Registered stocks and

shares become security by way of mortgage, which can be of two kinds—legal or equitable. The former type is the only method by which you can get a cast-iron unassailable security.

In the case of an equitable mortgage there is not only the danger of outstanding and older equitable interests ousting you from prior claim against the stock or shares, but while the borrower is still on the register as the owner of the shares, there is also the danger that behind your back he may deal with them to your detriment.

There is no uniformity of practice among banks as regards the type of mortgage which is taken, but the tendency is to have the security transferred and thus get the legal estate in cases where an advance is anything but purely temporary, or where the borrower is not known to be absolutely undoubted.

Legal Mortgage. Now, a legal mortgage of things other than land is accomplished by putting the property in the thing—that is, the legal ownership, remember—in the hands of the lender, who thus gets a legal estate, while the borrower has only an equity—that is, a right to redeem his property by paying off his debt.

In the case of stocks and shares, this means putting the bank or its nominees on the company's register as the owner of such stocks or shares. It used to be the practice to transfer them into the joint names of, say, a head office official and the local manager, but the modern method is to put them into the name of a nominee company, incorporated principally for this purpose.

The advantage of this procedure is that such a company has perpetual succession—it never dies—while bank officials retire and in due course die, with all the attendant bother of transferring the shares into fresh names.

This method of taking a legal mortgage—that is, of getting the shares transferred outright into the name of the bank's nominee, is, I have said, the only perfect form of security. There may be other interests in being, but

provided that at the time of transfer you were unaware of them—for example, that you did not have any idea that the shares were trust property—you have pride of place.

The rule as to priority of mortgages, other than mortgages of land, is the old one that "where the equities are equal, the law prevails," which in ordinary language means that where two or more parties have rights in the same property, priority is accorded to the one who has got the legal estate, in ignorance, of course, of earlier equities or rights.

There are two or three possible drawbacks to be noted in connection with a legal mortgage by transfer outright. Firstly, in the case of partly-paid shares, the bank, by becoming the registered holder, makes itself liable for any calls the company or its liquidator may make. This liability will not necessarily cease on the re-transfer or disposal of the shares, for Section 212 of the Companies Act, 1948, provides in effect that in the event of liquidation, if existing members of a company are unable to find the amount unpaid on their shares, any one who has been a shareholder within one year can be called upon to contribute such unpaid amount, provided that it is required to satisfy debts owing by the company at the time he was a member. For this reason, banks do not have partly-paid shares that may be taken by them as security, transferred outright, but prefer to take an equitable mortgage, leaving them in the name of the borrower.

The second possible disadvantage of having shares held as security transferred into nominees' names is a remote one, but, nevertheless, not to be overlooked. It arises from the fact that if you put a transfer forward for registration, you thereby vouch for its genuineness, and should it turn out later that the transferor's signature is a forgery, you will have to indemnify the company concerned for the loss it suffers in having to restore the original holder's name to the register.

The leading case on this point is *Lord Mayor, etc., of Sheffield* v. *Barclays and others,* which can be read in Volume 2 of *Legal Decisions Affecting Bankers.*

The facts were that one of two trustees raised money for his own uses on Sheffield Corporation stock standing in the joint names of himself and his co-trustee. The stock was transferred to a nominee of Barclays Bank, the fraudulent trustee forging his co-trustee's signature to the transfer. Later the stock was sold and the advance repaid, and when the fraud was discovered on the death of the delinquent, the surviving trustee claimed to have the register rectified in his favour, to which course the Corporation of Sheffield had no option but to agree. They, of course, could not remove the names of the transferees from the register, and so claimed to be reimbursed by Barclays Bank for the consequent loss.

Judgment was given by the House of Lords in the Corporation's favour, it being stated in the judgment that "the true contract to be implied from these circumstances (that is, the putting forward of the forged transfer by Barclays Bank) is not only a warranty of title but also an agreement to keep the person in the position of the appellants indemnified against any loss resulting to them from the transaction."

And there is this uncomfortable fact to be reckoned with—this liability to indemnify a company is not exhausted by the Limitation Act, 1939, for the Statute will not commence to run in your favour until the cause of action arises, which will be when the company has to replace the rightful owner on its register.

Certain companies—principally railway companies—have adopted the Forged Transfers Acts of 1891 and 1892, whereby they are empowered to raise a fund out of which to compensate holders of their stock or shares on account of forged transfers. Other companies take out insurance policies for such risks.

I imagine that when shares in joint names are offered

as security, most bankers have in mind not only the possibility of an irregular trust borrowing, but also the risk of a forged signature to the transfer, should the shares be transferred to their nominee, and consequently prefer to have the transfer executed by both parties in their presence.

Here is another possibility: John Brown, of whom you know little, brings you a share certificate in the name of John Alfred Brown and asks for an advance against it. You will no doubt notice the discrepancy in the names and ask for an explanation, which will probably be that Brown, originally baptised with two Christian names, has since shed one.

You may possibly as a precaution ask for a statutory declaration to this effect, but do not forget that if you have had the shares registered in your name and later on sell them to repay the advance, you will be the loser if it turns out that the shares in fact were the property of the borrower's father, whose signature had been forged.

Let no one think that this is apocryphal; it is a warning, founded on fact, to check a borrower's name in your books with his name on any registered securities offered as cover.

One other point must not be overlooked when a borrowing against a legal mortgage of shares is contemplated. In some few cases of public companies, the articles provide for the restriction of transfers to people engaged in particular trades and hence you may not be able to perfect your security by registration. Likewise, the articles of some companies preclude the registration of a limited company as a shareholder.

Now, as to the method of taking a legal mortgage over stocks and shares. A memorandum of deposit is executed under hand, setting forth, among other things, the purpose of the deposit of the shares and the conditions under which the bank's power of sale will arise, about which matters I will speak more fully presently.

A transfer is executed with a nominal consideration—usually five shillings—inserted, and presented with the relative certificate for registration at the company's office. The new certificate issued in the name of the bank's nominee will be kept at Head Office or the branch concerned, according to circumstances.

A transfer in respect of stocks or shares held as security for an advance requires only a 10s. revenue stamp instead of attracting *ad valorem* duty, falling into the category of exemptions from Section 74 of the Finance (1909-10) Act, 1910, and the Finance Act, 1947. Of course, duty-free stocks go free. The transfers in use by nominee companies usually certify on the back that nominal duty only is payable, and this will generally be accepted by a company registrar without adjudication by the Inland Revenue authorities.

In this connection I would point out that a cheap way is not opened up to escape *ad valorem* duty on the purchase of shares, for if a customer arranges for a purchase straight into the name of your nominee company, the relative transfer will require stamping at the full rate.

Once shares are transferred as security for an advance it will mean that all notices and dividends will come direct to the nominee company. There follows from this, that any notices concerning schemes affecting the borrower's interests must be passed on to him; for example, options to take up a new issue on favourable terms. Any loss arising in this connection from the bank's neglect will have to be borne by the latter. Dividends, of course, belong to the borrower, but it is of interest to note that, in the event of his bankruptcy, any dividends received subsequent to the receiving order can be used to keep interest on the debt on foot.

Equitable Mortgage. There now remains to be discussed the alternative method of taking an equitable mortgage over stocks and shares. Some of you will recollect that whereas a legal mortgage gives you rights

against the thing mortgaged, an equitable charge only gives you rights over the person—a right to have a legal mortgage executed or to share in the proceeds of sale.

An equitable mortgage of shares in its simplest form is accomplished by the mere deposit of the relative share certificate with intent to charge. Obviously, this method is fraught with many defects—there is no written evidence as to the purpose of the lodgment of the certificate, there are no explicit conditions as to realisation of the security, and the debt covered by the charge is not categorically defined. Nevertheless, you would get certain rights as an equitable mortgagee in such circumstances—the right to hold the certificate while the debt is outstanding, the right to go to the Courts for an order for foreclosure and sale.

Where the production of the relative certificate is not essential when shares are transferred, it is possible that the simple deposit of the certificate would not constitute an equitable charge. Such cases are rare indeed, and I imagine that pretty well every share certificate you see is marked at the foot to the effect that it must be produced on transfer. The better method is, of course, to back up the deposit of the certificate by a memorandum of deposit detailing the terms and scope of the charge.

In describing the principal features of the usual memorandum I would point out that its use is not confined to an equitable mortgage—it is used where a legal mortgage is taken by transfer of the shares outright, and it is also used where bearer securities are pledged.

The memorandum opens with a declaration that the items enumerated in the schedule at the foot of the form have been deposited as security. This shuts out the possibility of any assertion thereafter by a borrower that the shares were lodged for safe custody or any other purpose.

Then the debt secured by the charge is recited as advances made, or which may be made, so as to get a

continuing security. Otherwise, by the operation of the rule in *Clayton's* case, you might be left with a debt to which the security did not apply, for all payments to credit would be appropriated to wiping out the debt existing at the time of the deposit, and all payments out would be uncovered.

The debt is expressed in the widest possible terms to cover not only moneys owing on current account, but also sums due on account of bills discounted, guarantees, etc. The debt is also expressed in at least one bank form to cover moneys owing by a survivor or survivors in a joint account.

This is inserted out of abundance of caution to cover cases where security is lodged to secure a joint account by one of the parties who subsequently dies and no several liability has been established. For it might be argued that, inasmuch as the deceased's estate was released from liability for the joint debt, so also was the security lodged to secure the joint debt.

Then there will be an undertaking to maintain a specified margin of cover, dependent, of course, on the type of security offered. This is followed by a power of sale over the security in the event of default or breach of any of the covenants.

This power is only effective, of course, if the shares have been transferred or completed transfers or effective blank transfers are held. If the power of sale is not expressed as immediate, then reasonable notice will have to be given of the intention to sell (*Deverges* v. *Sandeman*, [1902] 1 Ch. 579).

To cover cases where the stocks and shares are untransferred, a covenant will be found whereby the borrower undertakes to execute any necessary transfers for putting the security into the name of the bank or its nominees or for vesting it in a purchaser. Experience shows that borrowers are anything but agreeable to implementing this undertaking if the bank wishes to perfect its security or to sell it.

Then, in at least one form, there is a final agreement phrased something like this: "I agree that on a release by you to me of any of the said stocks, shares or securities I will accept delivery of stocks, shares or securities of the same class and *denomination* as those hereby charged."

This cryptic clause is inserted to cover a situation such as arose in the Scottish case of *Crerar* v. *Bank of Scotland*, [1921] S.C. 736. Here a lady borrowed on the security of shares in J. and P. Coats, Ltd., which were duly transferred into the bank's name. On repayment of the advance, a number of shares was retransferred to the lady equivalent to those she originally lodged. You will readily understand that the Bank of Scotland always had a large block of these well-known shares standing in their names for advance purposes, and it happened that the shares handed back to their customer were not the identical shares she had lodged. But for some reason she claimed that she was entitled to get back the actual shares she had charged, and if the Court had not found that she had, in fact, by her conduct, waived her right to these self-same shares, it appears that the lady would have succeeded in her action.

Hence the presence of the clause I have just quoted to you, which obviates the necessity of setting up machinery for ensuring that each separate holding is earmarked while standing in the name of the bank or its nominees.

This matter is not now of such moment inasmuch as Section 74 of the Companies Act, 1948, provides that where all shares of a particular class are fully paid and rank *pari passu* for all purposes they need not bear a distinguishing number.

Lastly, a schedule is completed of the items that are lodged, and this is followed by the signature of the party charging the security. If the signature is above the schedule, then the latter should be initialled by the depositor of the security.

Where a borrower is continually changing his invest-

ments, it is a laborious business to be constantly cancelling letters of deposit in respect of securities sold, and taking fresh ones in respect of securities bought. In such cases it is not uncommon for a sort of "omnibus" charge to be taken over existing and future holdings of stocks and shares, and this is done by the memorandum of deposit charging, instead of specific items, "all the securities now and/or from time to time lodged by me with you in addition thereto or in substitution therefor."

Alternatively, a form of general charge, as used in the case of stockbrokers' loans, is adapted, which reads something like this: "All stock and marketable securities of any class from time to time lodged with the above-named bank or transferred to its nominees by or on account of the undersigned, shall remain as a security for the payment to the bank of all moneys from time to time owing by the undersigned," etc.

If you do take such a general charge, I suggest that the items of security, as and when they come into your hands, should be entered in your security register. Also, that any items in your safe custody books which you want to get within the ambit of your charge should be transferred to the security register, so as to make it plain beyond all dispute that they did not come into your hands for the specific purpose of safe custody.

The memorandum of deposit will require stamping as an agreement under hand with a sixpenny stamp, which can be adhesive if affixed at the time of execution of the form, or can be impressed within 14 days of its date If the borrower is a limited company, the memorandum can be signed under the hand of duly authorised officials and then attracts duty at the above rate.

In this case, you will require to file with your security a certified copy of the resolution of the Board, authorising the officials in question to execute the form. If, on the other hand, the seal of the company is affixed to the memorandum, stamping will be required within 30 days

at the rate of 5s. per cent on the highest amount it is proposed to advance.

This, then, is the essence of an equitable mortgage of stocks and shares—the deposit of the relative certificate accompanied by a memorandum of deposit.

Let us look now at the defects of this type of charge, and the precautions you can take to counter them. Obviously, the fundamental disadvantage is that you have not got the legal estate; you have only got a right to call for it—for that is what an equitable charge amounts to—or a right to get your debt satisfied out of the proceeds of sale.

Now, the risk attaching to a mere equitable interest is that it is liable to be overridden by an earlier equity even if you had no notice of it. For the law regulating the order of equitable interests, other than interests in land, is that priority is accorded to the earliest equity or right. In other words where several parties all have interests in the same shares, the date order of their interests will settle the order in which they can claim on the proceeds of sale.

Let me give you a concrete case. A customer borrowed by way of equitable mortgage against shares duly registered in her name. Later it transpired that she held the shares as trustee for her children, so that when the bank wanted to enforce its security, it was faced by a hostile claim. Here there were two equitable interests in the same shares—that of the bank who had lent money on them and that of the children who were the beneficiaries under a trust. Theirs was the earlier equity, and so it prevailed against the bank's equitable interest.

I cannot see that there is any way of guarding against this risk if you are content to leave the shares in the borrower's name; the share certificate will not disclose any fiduciary interest, for a company, as we shall see, will not record any trust interests on its share register.

Then the next drawback is that when your power of

sale arises and the borrower fails to keep his covenant to execute a transfer, you are faced with the cumbersome, costly and lengthy business of resort to the Court for an order for foreclosure and sale.

To obviate this tedious process, it is the fashion to get your customer to execute a transfer which you file with your security, and do not register. In some cases a completed transfer is taken in which the bank is named as transferee.

Such a transfer will require stamping with a nominal duty of 10s. and it is difficult to see why, having got thus far, the transfer is not presented for registration and a legal mortgage taken. Possibly the reason is that the borrower is sentimentally disinclined to have the shares taken out of his name.

When such a transfer duly dated is at length put forward for registration on default of the borrower, the company may query the transaction, but there seems to be no valid reason why such a transfer, though stale, should not be accepted for registration.

More usually a blank transfer is taken, and it is necessary, first of all, to appreciate exactly what is meant by this term. A blank transfer is one whereon some material particular is lacking—such as the name of the transferee. I should like to point out that the mere fact that the date is lacking on the instrument does not make it a blank transfer, for the effective date of a document is the date on which it is executed, not necessarily the date it bears. The idea of taking a blank transfer, of course, is that, if necessity demands at a later date, the blanks can be filled in and the shares sold. Whether this is effective depends on the regulations of the particular company concerning its transfers.

For example, companies governed by the Companies Clauses Consolidation Act, 1845, such as public utility concerns, require their transfers to be by deed—under seal—and a good many companies formed under the various

Companies Acts have the same provision in their Articles. Now, if such be the case, a blank transfer is of no use, for a deed to be effective must be complete at the time of delivery—that is, when the borrower hands over the transfer—no material particular must be lacking. For such a transfer to be valid, it will require re-delivery by the borrower after you have completed the missing details —a formality that will generally be impracticable.

Alternatively, to regularise matters it would be necessary for the borrower to give you a power of attorney to fill in the lacking particulars, and as this would authorise acts to be done under seal, such power would itself have to be under seal, and is equally impracticable.

You might complete the transfer and get it accepted by the company, which would probably have no inkling of the fact that the instrument was inchoate at the time the shareholder delivered it to you. If you got yourself registered you might think you were safe with the legal estate in your hands, but you would not be; for the legal estate can only be acquired through a regular and valid instrument of transfer.

The leading case on this point is *Powell* v. *London and Provincial Bank*, [1893] 2 Ch. 555, reported in Volume 1 of *Legal Decisions Affecting Bankers*.

Here a fraudulent executor deposited some stock in a statutory company with a bank as security for an advance. The stock was left in his name and a blank transfer taken. The following year, in the absence of a reduction in the overdraft, the bank proceeded to complete the transfer and got itself registered as owner of the stock. Four years later the borrower absconded, and the trustees appointed in his place claimed that the bank held the stock in trust for them and had no sort of beneficial interest therein.

The Court upheld their claim on the following grounds: The company in question being a statutory company, its transfers had to be by deed, and a document under seal

executed in blank, such as the transfer in this case, was not a legal or effective deed. There had been no redelivery of the transfer deed by the fraudulent borrower after it had been completed by the bank, neither was the bank authorised by deed to complete the missing details of the transfer. Consequently, the bank had not in fact got the legal estate, but merely an equitable interest, which was postponed to the earlier interest of the beneficiaries.

If there is nothing statutory, or in the articles of association of a company, which makes a transfer by deed necessary, a blank transfer is effective, for the delivery of an instrument under hand authorises the transferee to fill up all necessary blanks, and it thereupon operates as a good transfer without redelivery (*Ireland* v. *Hart*, [1902] 1 Ch. 522).

The articles usually prescribe that a transfer of a company's shares shall be in the common form, which is under hand, and not under seal. Article 18 of Table A says that shares shall be transferred in any usual or common form which the directors shall approve, or in accordance with a formula given at the end of the article, a formula that is under hand.

This is what Palmer has to say on the matter in one of his works on companies—

> "The instrument of transfer must be in such form, if any, as the articles provide. They generally prescribe the usual common form. Sometimes the regulations say that the transfer must be by deed, but Table A, new or old, only requires the transfer to be in writing, and companies which require a deed are quite in the minority. Where no seal is requisite, the fact that a transfer, if in other respects regular, is under seal will not invalidate it. It is, however, always well to follow, as nearly as may be, the form, if any, prescribed by the articles."

Now I suppose that pretty well every transfer you

meet with appears to be a deed; there is the little red seal and the usual formula about signing, sealing and delivering. Possibly this suggests to you that any such transfer is ineffective unless complete in all respects as a deed at the time it is delivered; but provided there is nothing in the statute under which the particular company was incorporated, or in its articles, ordaining that a transfer must be in deed form, you can disregard the seal and treat the instrument as having been executed under hand. This means that it can be taken in blank and completed at a later date and duly registered, giving you a legal title to the shares.

Lien. There are other possible risks involved if you do not get the legal estate in the shares by having them transferred. For example, when you come to enforce your security you may find yourself in competition with the company concerned, which claims a lien over the shares in question on account of money due to it from the shareholder.

To provide against this contingency, you serve a notice of lien on the company when you take untransferred shares as security. In some few instances you get an acknowledgment and a request for a registration fee of, say, half-a-crown. In most cases your notice is either ignored, or a formal reply is sent in the case of an English company, pointing out that the company, by Section 117 of the Companies Act, 1948, can take no notice of any trust, express, implied or constructive, although, in fact, I understand that a sort of unofficial register of such notices is kept.

Now, what are you going to do in face of such a rebuff? If the company repudiates the efficacy of your notice, it at least cannot afterwards aver that it never received it; if no reply is received to your notice of lien and you want to persist, send a further one by registered post.

Sometimes Section 117 is enlarged by the articles of association providing that the company shall have a first

and paramount or permanent lien on its shares for any moneys owing to it by the shareholder. You should note in this connection that Article 11 of Table A, of the 1948 Act, which provides for a lien on shares, only applies to partly paid ones.

In the face of all this, it might appear to be a waste of time and stationery to bombard companies with notices of lien, unless their repudiation is based on false premises. The fact is that the company must be regarded as functioning in two ways—as a registering body and as a trading entity. In its first capacity it is bound by statute not to put any trust interests on its register—it is not going to hold the scales between competing interested parties in the shares. But in its second capacity, as a trading concern, it may acquire some charge on its shares for a trading debt owing by a shareholder, in which case it is pretty well in the position of a first mortgagee. Thus, when it receives a notice of lien from a third party, such as a bank, it cannot take priority for any debts incurred by its shareholder subsequent to such notice.

The case of the *Bradford Banking Company, Ltd.* v. *Henry Briggs, Son and Co.* (1886), 12 App. Cas. 29, reported in *Legal Decisions Affecting Bankers*, Vol. 1, is the authority for saying that a notice of lien given by a bank as chargee of a company's shares effectively warns the company in question that it cannot enforce its lien over the shares at issue in respect of after-incurred debts of the particular shareholder.

There a shareholder in the defendant company, from time to time deposited share certificates as cover for advances with the appellant bank, who only gave notice of lien to the company. The latter acknowledged the notice, but added a warning that its shareholder was indebted to it, and that under its articles of association it had a first and permanent lien on his shares. When the shareholder went into liquidation, he was a debtor to the company for a considerable sum and the question arose

whether the company could exercise its lien in respect of sums lent after receipt of the bank's notice.

The case was settled in the House of Lords in the bank's favour on the following lines: The words in the articles of association, "first and permanent lien," merely made the company first mortgagee of the shares of any shareholder who might be indebted to them; as first mortgagee the company was at liberty to make further advances to its shareholder until it received notice of a second mortgage, after which event it could not make further advances to rank in front of the interest of which it had received notice; the notice of lien given by the bank was not notice of a trust which the company was by statute forbidden to recognise, but was an effectual warning to the company that the remanent interest in the shares had been charged to the bank.

You will probably say that the cases where a borrowing customer is also indebted to the company in which he has shares are few, and that, consequently, the service of notice of lien is a meaningless formality in the ordinary way. In cases where you are dealing with fully-paid shares that enjoy an official quotation on the London Stock Exchange, there is small point in sending a notice of lien to the secretary of the company in order to protect yourself as against the company, for by the Rules of the Stock Exchange a condition of an official quotation is that no lien shall be claimed by a company on its fully-paid shares. Some banks, accordingly, refrain from sending notices in such cases.

I suggest that where you are not concerned with fully-paid officially quoted shares, a notice of lien is in some instances an essential precaution to take. A case in point occurred where a publican borrowed on brewery shares, which were left in his name; a blank transfer was taken, but no notice of lien served on the brewery company concerned. When the bank came to enforce its security it found that its publican customer was heavily indebted to

the brewers for stock supplied, and the latter successfully claimed to stand in front of the bank, for its articles gave it a first and paramount lien and it had not received notice at any time of the bank's interest in the shares.

Another typical instance where notice should be given is in the case of advances against partly-paid shares in another bank, for it is conceivable that your customer is borrowing from such other bank also on the strength of his shareholding. Although a bank will usually refuse to recognise your notice of lien, it would appear that it could not rely on its lien on its own shares for advances made after your notice was in its hands.

There is at least one bank whose articles give a paramount lien on its shares for all liabilities incurred by its shareholder before and after receipt of notice of lien from an outsider. It is doubtful, however, if a company, by such a clause in its articles, shutting out all equities, can get any further protection than is given in Section 117.

Notice of lien will only operate to determine your position in competition with the company; if there were earlier equitable interests, they would have a prior right over you even if they had not been notified to the company. For as between successive equitable interests, priority is determined by the date of their creation and not of notice to the company, which is not a registering body in this sense.

But there is another risk, when lending against untransferred shares, which may be guarded against by means of a notice of lien—I refer to the possibility that your customer has obtained a fresh certificate from the company by representing that he has lost or destroyed the original. As you know, a company will usually issue a duplicate against a satisfactory indemnity sometimes accompanied by a statutory declaration by the shareholder, stating that the shares are not the subject of a charge elsewhere.

If an unscrupulous borrower got a fresh certificate by this means, he could then sell the shares and leave you

to fight the matter out with the company when you come to realise your security. But if you had given the company notice of lien it is probable—although the point has never been raised in the Courts—that the company would be at fault if it did not advise you, when you put your notice in, that the shares had already been sold by means of a duplicate certificate, or let you know at a later date should the borrower try to get a fresh certificate. This is the view taken by Mr. Bernard Campion, K.C., whose authoritative remarks on the whole question of lien can be read with profit in the *Journal of the Institute of Bankers* for December, 1928.

While dealing with the question of lost certificates, I would remind you that the giving of an indemnity to a company by a bank on behalf of a customer is not, as some people imagine, a mere formality on account of the non-negotiable nature of a registered certificate. Such indemnities should only be given in cases where the parties concerned are absolutely undoubted for the counter-indemnity that is usually taken.

Apart from deliberate fraud on the part of a customer, it is quite possible that he, or more likely she, may genuinely be under the impression that the certificate has been lost when all the time it is in other hands. I can recall an instance where a lady got a fresh certificate on a bank's indemnity, under the honest conviction that she had lost the original document, when as a matter of fact she had raised money on it years previously with a firm of solicitors.

If it were not for the unfortunate, unbusinesslike and muddleheaded habits of a certain type of lady customer, this would read more like a fable than a statement of actual fact. But that is a case taken from practice: therefore, you should be particularly careful, when giving an indemnity to a company in respect of a new share certificate, to make sure that the counter-indemnity is taken from someone who is worth powder and shot.

There are two further and effectual methods of protecting your interest in a customer's holding of shares, methods which are only invoked in exceptional cases.

Notice in Lieu of Distringas. The first is by serving what is called a notice in lieu of distringas on the company. This is done under Rule 4 of Order 46 of the Supreme Court, which provides that a party claiming to be interested in shares registered in the name of another, may file a notice of the matter, together with an affidavit, in the Central Office of the Supreme Court or at a District Registry. An office copy of the affidavit and a sealed duplicate of the notice will be supplied to the deponent, who will then serve it on the registered office of the company concerned.

The effect of such a notice is that the company must give you eight clear days' warning of its intention to pass a transfer of the shares, thus giving you the opportunity of taking further steps to protect your interest, usually by applying for an injunction in the High Court. If you do not take action within the eight days the company can proceed to register the transfer.

The notice can also be drawn to restrain the company from paying dividends to the shareholder. A fee of 10s. is chargeable for filing a notice in lieu of distringas, and, of course, there are the commissioner's fees when swearing the affidavit.

This method of blocking any dealings in shares in which you are interested is not often resorted to. It might be used where untransferred shares were the subject of an advance and you have reason to suspect the good faith of your customer. Another instance is found where advances are made against a mortgage of a customer's equitable interest in an estate which includes stocks and shares—an interest arising out of a trust for sale or a reversion. As mentioned on page 187, notice of such mortgage should be served on the trustees in whom the assets of the estate are vested, but where shares or stocks are

concerned you can also, as a precautionary measure, serve a notice in lieu of distringas on the several companies, so that if and when the trustees proceed to realise the estate you will hear of it.

Charging Order. Then there is a charging order, by which a company is restrained from allowing dealings with a specified shareholding. This can only be obtained by a judgment creditor. Where judgment has been obtained against a debtor and it is unsatisfied there is, as you know, a variety of remedies open to you.

You can issue a bankruptcy notice which warns the debtor that he will find himself involved in bankruptcy proceedings if he does not do something within seven days. If you know he has funds in a third party's hands you can try to attach them by means of a garnishee order. You can get execution levied against the debtor's goods and chattels. And, if he is possessed of real property, you can attach it by means of a writ of elegit.

If you are aware that the judgment debtor holds stocks and shares, you can tie them up by means of a charging order, which, when made absolute, takes effect in the judgment creditor's favour as from the date of the order nisi.

You will appreciate that this method of getting at a debtor's assets in the shape of stocks and shares would only be resorted to where you had no existing charge over them. If this were the case, your remedy would lie in the sale of the security without or with the aid of the Court, according to whether you had a legal or equitable charge.

Probably you are more usually concerned with a charging order in different circumstances, where shares are held by you as security and a judgment creditor of your customer applies for and gets a charging order on the same shares. On receipt of notice of this you should not make further advances on the strength of the shares in question, but you are entitled to hold them against the debt existing at the time you had notice.

A charging order absolute "only effects a charge upon such interest as the debtor had in the property at the date of the order nisi." The debtor's interest would clearly be subject to your charge.

Private Companies. Shares in private limited companies are not an acceptable form of cover for many reasons, and it is only in exceptional cases that they are taken in support of an advance. To begin with, a private company must in its articles place a restriction on the transfer of its shares—often you will find that they must be offered in the first instance to existing shareholders.

This means, firstly, that there will probably be no chance of the bank getting the shares transferred into its nominee's name, and secondly, that even if an effective blank transfer is taken, you cannot easily realise your security—there is no freedom of transfer. Furthermore, even if you could get on the register it might happen that the registration of your nominee as a shareholder would be irregular in that it brought the number of members, apart from employees, to over 50, which is forbidden by the Companies Act, 1948, Section 28.

You may think it advisable to serve the company with notice of lien, but experience shows that the borrower usually takes exception to this formality, because, the company being often a family concern, he is not anxious for his affairs to be known to his relatives.

A further defect of such shares as security is that it is difficult to put a value on them. It is true that the rate of dividend paid will be some sort of criterion and that the secretary of the company will usually quote the figure at which they last changed hands. But it must be remembered that this may not represent their true value, as a member of the company may be engaged in paying an inflated price in order to get a controlling interest.

Possibly you will check the price obtained in the above ways by treating the company's balance sheet on a break-up basis—that is, by estimating the surplus remaining

after the real liabilities have been deducted from the forced sale value of the assets, and seeing what each unit of the several classes of shares would receive back on liquidation.

Company Customers. When you happen to lend to a limited company against the security of stocks and shares, the possibility of such security being the subject of a charge in a debenture held elsewhere must not be overlooked. If you take your security before such a debenture is issued, your priority is untouched, whether the shares are transferred into nominees' names or not.

If a debenture is subsequently issued giving a specific charge on the shares in question, notice of the fact would involve breaking the account in order to maintain priority for the advance existing at the time you received notice—you would be a first mortgagee in receipt of notice of a second charge. In this connection it is possible that registration of the debenture at Bush House would be deemed to be notice to you; hence, keep a vigilant eye on *Perry's Gazette* or similar publication.

If the debenture only creates a floating charge there will be no need to break the account. If, however, you take a charge over stocks and shares held by the company, subsequent to the issue of a debenture by it, you would be postponed to any specific charge over the stock and shares contained in the debenture, for although such specific charge might only be equitable, it would be earlier in time.

Should the debenture only contain a floating charge, your charge, even though created later, would take precedence, for a floating charge leaves the company free to charge its assets in the ordinary course of business until crystallisation takes place. But most floating charges contain a condition that "the company is not to be at liberty to create any charge on its assets ranking *pari passu* with or in priority to this debenture."

Would the existence of this clause affect your priority?

The answer is: Only if you knew of the existence of such conditions, and the fact that you searched the register at Bush House would not fix you with notice of this condition, unless it was included in the details of the debenture registered in the company's file.

Repayment of Advance. When an advance against Stock Exchange securities is repaid, the security can be vacated with a minimum of formality. If you are dealing with bearer bonds, they only require to be delivered to the pledgor and the memorandum of deposit cancelled.*

Likewise, registered certificates left in the borrower's name only require to be returned to him and the memorandum and any transfers cancelled. If notice of lien has been given, it is as well to notify the company that you withdraw it, in order to save your customer trouble when he comes to sell the shares.

If the security consists of inscribed stocks or registered stocks or shares transferred into the name of the bank or its nominee, it will be necessary to retransfer them into the name of the person who lodged them, such transfer attracting the ten shillings stamp duty. It is not infrequent in the case of stockbrokers' loans for a letter to be addressed by the borrower to the bank directing the latter to hold at the disposal of a third party specified items of stocks and shares standing in the name of the bank's nominee company.

On occasion the question has arisen as to whether these "bank letters" attract stamp duty. I understand that in practice they are not stamped and that legal opinion is behind such practice, as such letters are merely a direction to a trustee by the party creating the trust to deal with the trust property in a prescribed way.

But when the stocks or shares are eventually transferred at the direction of the third party, *ad valorem* stamp duty will have to be paid, as will be the case whenever items held in a nominee's name are transferred to any

* But see page 191.

other party than the one who originally lodged them or his legal personal representatives as such.

Realisation of Security. Now, as to cases where a bank has to realise its security on default of the customer.

In the case of a pledge or a mortgage, there is an implied power of sale, and so, whether it is a case of a pledge of bearer bonds or a mortgage of shares, you have your remedy of sale on default in payment. If a time is fixed for payment, default takes place on failure to pay at that date, and if no time is fixed for repayment, then reasonable notice must be given before the power of sale is exercised.

What is reasonable notice depends on the facts of each particular case. These points emerged from the case of *Deverges* v. *Sandeman, Clark and Co.* (*supra*) (*Legal Decisions Affecting Bankers*, Vol. 2, p. 23).

As before mentioned, the typical memorandum of deposit used by banks covenants for repayment on demand and provides for an immediate power of sale. In practice it is usual to give a borrower as much latitude as circumstances make desirable—having regard to such matters as falling markets.

If it is a case of bearer security, it can be sold with a minimum of formality. If stocks or shares in your nominee's name are at issue, they can be sold out of such name. But if stocks or shares are held with a blank transfer, it will be necessary to have the shares put first of all in your nominee's name by the completion of the transfer and then to sell out of such name, in cases where your nominee's name was inserted as transferee when the blank transfer was taken.

If no blank transfer is held and the borrower will not co-operate with you, you are thrown back on recourse to the Court for an order for foreclosure and sale—a costly and a tedious business.

Where the borrower is involved in bankruptcy, and the shares are untransferred, you will not be faced with resort to the Court, for the trustee will sign transfers as

the legal assignee of the bankrupt's property—the company having been duly furnished with evidence of his authority. The same considerations apply, of course, to a trustee under a Deed of Arrangement.

If you have a blank transfer signed by the bankrupt borrower, it is unwise to complete it and register it with the company, who are in ignorance of their shareholder's bankruptcy—the trustee is the proper person to act.

CHAPTER VIII

LIFE POLICIES

> "A banker should never make advances upon life policies. They may become void, should the party commit suicide, or die by the hand of justice, or in a duel; or if he goes without permission to certain foreign countries. The payment may be disputed, upon the ground that some deception or concealment was practised when the policy was obtained. And, in all cases, they are dependent upon the continued payment of the premiums."—*The Logic of Banking*, by J. W. Gilbart.

GILBART'S categorical condemnation of life policies as security has a strange sound in these days, when a policy with a good surrender value issued by a British office of standing is regarded as a welcome item of security free from most of the defects attaching to other forms of cover. The author's morbid apprehensions of a violent death with its annulling consequences on the security find little place in the modern banker's estimate of a life policy as security. Possibly there was some warrant for Gilbart's gloomy views some eighty years ago, when there were but few first-class companies specialising in life assurance, and when there was little variety in the type of policy issued.

To-day there is a large number of first-class companies in the field specialising in life cover, and they will issue a policy to cover practically any particular case. So it is now no exaggeration to say that a life policy issued by a first-class company, and having some sort of a surrender value, is regarded as being in the front rank of banking security. Ready realisability is always present and there is no fear of being left with a depreciating security—on the contrary, a life policy steadily increases in value with each premium that is paid.

Where a policy has no immediate surrender value, it is, on occasion, nevertheless a welcome piece of security, and, in some cases, one that should be insisted on. As a backing to the guaranteed advance of a professional man, or in cases where a trader has no free assets to charge and you are content to lend while the business is a going concern—which implies the continued existence of its owner—a policy duly charged is desirable, if not essential.

Possibly, the two defects in a life policy as security are, firstly, the necessity for keeping the policy alive when the borrower cannot pay the premiums and the position does not make the surrender of the policy expedient. Of course, it is possible in some cases to exchange the policy for a paid-up one. But even if the banker has to provide the premiums it will be found that the value of the policy occasionally increases by more than the amount of the premium paid, and in any case the payment of premiums does not mean that the money is thrown away—you are getting an improving security.

The second possible defect is that a policy of life assurance, being a contract of the utmost good faith, any misrepresentation or wilful withholding of facts by the assured at the time the policy is taken out may involve repudiation of liability by the company, and this is, of course, a risk, remote though it may be, over which you have no control.

Life Assurance Policy as Security. Let us now look at the considerations to be borne in mind when accepting a life policy as security.

Firstly, the standing of the company concerned is of some importance. While the majority of British life companies present a position of absolute stability and safety, there are a few who are not in this position. Policies in companies domiciled abroad with no English office are not favoured on account of the trouble involved if the policy becomes a claim or is surrendered. Policies issued by Colonial and Dominion companies are not put

in the same category by some people as those issued by English companies, owing to the different practice in the employment of funds.

Then the type of policy offered requires consideration. At the present time, when people are becoming increasingly "insurance minded," the different types of cover offered are legion. I will only remind you that a banker prefers an endowment policy to the whole-life type, because there is a definite maturity date in the case of the former, while the latter type may involve you in a lengthy wait and a long standing advance—the sort of case where your inquiries as to your customer's state of health have more than a conventional significance.

Of course, a paid-up policy, especially of the participating variety, is the ideal security, as it progressively increases in value without any corresponding outlay. A "closed fund" policy is best of all—usually increasing in value at a more rapid rate than the ordinary type. Such a policy is found in cases where a life office has been absorbed by another company and no new business is taken in respect of the existing assets of the merged office.

Then the policy should be carefully perused to see if any restrictions are imposed on the life assured. Occasionally qualifications are made with regard to foreign residence or to air travel; if a life is accepted without a medical examination, something may be said about the amount payable if death occurs within a specified period. In the case of some industrial policies, it will be found that the face value is seriously diminished if death takes place within, say, five years.

Frequently you will find a suicide clause, providing that the assured's death by his own hand within, say, twelve months of taking out the policy will invalidate it. Where a policy provided that, if the life assured died by his own hand whether sane or insane within one year from the commencement of the insurance, the policy should be void against any person claiming the insurance moneys

and the assured committed suicide some nine years after, it was held that it was contrary to public policy for the contract of insurance to be enforceable against the company. (*Beresford* v. *Royal Insurance Co. Ltd.*, [1938] 2 All E.R. 602.) As a matter of fact, most policies usually provide that a suicide clause will not adversely affect the rights of third parties acquired by assignment for value.

Then you should make sure that the policy-holder has power to assign his interest. While most companies do not prohibit such action, it will be found that industrial policies are usually unassignable without the company's consent. Indeed, if they can be so dealt with, they are awkward things to take as security, as the premiums are usually payable weekly or monthly, which involves considerable trouble in keeping an eye on premium payments.

The policy must be examined to see if the assured and the life assured are identical, for when taking a policy as security you must be sure to get all interested and material parties to join in the charge.

A policy, whether payable at death (a whole-life policy) or at the end of a fixed term or earlier death (an endowment policy), may be payable to the assured, or his personal representatives, or to another person absolutely or contingently on such other person surviving the life assured or being alive on the maturity of the policy. If there is such a third person, he or she must be of full age and become a party to any charge you take.

The usual case you meet with is where a husband takes out a policy on his own life for the benefit of his wife, and on occasion a wife takes out a policy on her own life for the benefit of her husband. Now, if the policy merely mentions that the contract is in favour of the wife of the life assured, without mentioning her by name or using any expression which would limit "my wife" to "my present wife," a second wife would become entitled to the policy moneys.

In such a case, the policy definitely cannot become an acceptable banking security, for it is not possible to gather in all interested parties in the shape of subsequent wives. Any charge would only be effective if the first wife joined in the charge and survived her husband, or if she predeceased her husband and he either reverted permanently to single blessedness or succeeded in surviving any further partners that he espoused.

This follows from the principle laid down in *In re Browne's Policy*, [1903] 1 Ch. 188, which concerned a policy taken out for the benefit of the wife and children of a man, without naming any of them. It was held that the second wife and her children were entitled to share with the children of the first marriage to the exclusion of the executors of the first wife.

Where the wife is specifically named as beneficiary of the policy, the position is governed by Section 11 of the Married Women's Property Act, 1882. This provides that a policy on the life of a husband for the benefit of his wife and/or issue, creates a trust in favour of the beneficiaries, and as long as any absolute or contingent interests are outstanding the policy moneys do not form part of the estate of the life assured.

In the case of *Cousins* v. *Sun Life Assurance Society*, [1932] W.N. 198, the plaintiff insured his life for the benefit of his named wife under the provisions of the Married Women's Property Act, 1882. His wife predeceased him and her executors claimed the benefit of the surrender value of the policies.

In the first Court it was held that while the policies created a trust in favour of the wife, her interest was contingent on her surviving her husband, and hence the trust failed for want of a continuing object. In the Court of Appeal this decision was reversed, and it was held that the wife had a vested interest, and that, therefore, on her predeceasing her husband, the policy moneys passed under her will. It therefore follows from this decision that in

cases where a wife is named as beneficiary of the policy, she must charge her interest therein jointly with her husband.

It is not unusual for the policy to be expressed for the benefit of the wife and/or children duly named, and in such cases the children, if of full age, must likewise charge their interest. If any are minors, they cannot, of course, create any sort of charge over their interest.

The above types of policy must be distinguished, however, from the type where a wife is the grantee of a policy on her husband's life. Provided she pays the premiums no trust interest is involved and she can validly charge the policy in her own right.

Then occasionally a parent takes out a policy as agent for an infant child. In such a case, any charge given by the parent would only be effective on the child dying during his minority—if he attained the age of 21 the policy would become his absolute property. An insurance company in such cases will only lend on the policy for the purpose of paying the premiums.

Likewise, children's deferred policies are not good security, and life companies will not advance on them on account of the obscure position when the assured attains mature years. Such a policy would only be an effective banking security during the minority of the assured; on his majority his assent would be necessary to a continuance of the advance against the security.

You must distinguish between a policy taken out by a parent in his own name as agent for his child and a policy taken out by a parent for the benefit of his child on attaining a specified age. In the latter case no legal estate is created for the child, and the parent does not constitute himself a trustee for the child of the policy or the moneys payable thereunder. If therefore the parent dies before the policy matures, the surrender value belongs not to the child, but to the parent's estate and will be paid to his legal personal representatives. In the case of

Tibbetts v. *Engelbach*, [1924] 2 Ch. 348, a father, in the proposal form, said he was making the proposal for his child, and it was held that this was not entering into the contract as agent for the child, but for the benefit of the child.

All this will show you the necessity for a careful scrutiny of the contents of a policy offered as security, for, unless you have got in all interested parties, you may find your security worthless, or much less valuable than you imagined.

Now, as to the procedure to be adopted in perfecting your security.

Legal Mortgage. A life policy becomes security by way of mortgage, which can be of the legal or equitable variety, and we will take the legal mortgage first. A legal mortgage of a thing, with the exception of land, is accomplished by putting the legal ownership of it—the legal estate—in the hands of the lender, the borrower being relegated to an equitable interest in the shape of his equity of redemption, his right to get the property back.

A life policy is a chose in action; that is, a personal right to property which can only be claimed or enforced by action and not by taking physical possession, and thus a lender's security by way of mortgage of a life policy will consist of an assignment of the borrower's rights therein with a proviso for redemption.

Most banks have printed mortgage forms to cover a variety of transactions with life policies, such as a mortgage by the borrower himself, a mortgage by two or more parties, and a mortgage by a surety, and you should be very careful to see that you are using the form that fits the particular case and the type of policy.

The usual form of mortgage is expressed as a continuing security to avoid the adverse operation of the rule in *Clayton's* case, and is drawn to cover all possible liability to the bank on the part of the borrower. The policy, the details of which are enumerated, is duly assigned to the

bank, together with any bonuses and additions thereto, and the bank is empowered to give a discharge on behalf of the borrower's personal representatives for all moneys due under the policy, to prevent any difficulty arising where the amount of the debt is less than the amount due under the policy.

Authority is given for the bank to surrender or sell the policy at its discretion towards satisfaction of the advance, and the borrower undertakes duly to pay the premiums and to produce the receipts therefor. He further agrees that if the premium payment is a specified period in arrear, the bank may pay the amount to the debit of his account. In this connection arrangements are usually made for the periodical inspection of the receipts.

The form of charge, being a legal mortgage by deed, will require stamping at the rate of five shillings per cent on the highest amount it is proposed to lend—assuming the form is unlimited—or on the limit inserted in the form. You should note that the basis of stamping must not be the value of the security—in this case the surrender value, nor yet the face value of the policy.

As often happens, two policies may be charged at the same time, or a policy may be lodged additionally to title deeds. You can then stamp one of the mortgages collaterally to the other, or the mortgage of the policy collaterally to the mortgage of the title deeds—assuming that you are using "all money" charges under seal.

You should be careful to see that at all material times the charge form is stamped to cover the highest amount of the advance, for the company will require a certificate to this effect should the policy become a claim or be surrendered.

In *Re Waterhouse's Policy*, [1937] 2 All E.R.91, a policy for £500 had been assigned to a bank as security for an overdraft and the assignment was stamped to cover £500. In fact, the overdraft both at the time of taking

the policy as security and at the time of the maturity exceeded £500. The moneys payable at maturity, including a bonus, amounted to £963. The Insurance Office contended that the assignment was insufficiently stamped and therefore they could not get a good discharge for the policy moneys by paying them or any part thereof to the bank. On the other hand, the bank contended that it could give a good discharge for £500 and sought to get this sum paid over to it and the balance to the policy holder. It was held that under the Stamp Act, 1891, ss. 88 (2) and 118 (1), the assignment was a good security for £500 and the bank was entitled to be paid £500 out of the policy moneys.

You will, of course, have to value your security, and this is done by getting the surrender value figure from the insurance company, although some offices, particularly Colonial and Dominion companies, give a table of surrender values in the policies. A rough estimate for whole life policies is 30 per cent of the premiums paid after five years, rising to 40 per cent after 15 years, and to 60 per cent after 30 years, with higher percentages for endowment policies.

After the completion of your mortgage, notice thereof should be given to the company concerned, for by the Policies of Assurance Act, 1867, notice of any assignment of a policy must be given to the relative company, in order to get any rights under the policy, and the date of receipt of notice regulates the order of successive interests in the same policy. It is usual to send the notice in duplicate with a request that one copy shall be returned, duly acknowledged by the company, which is entitled to a statutory fee of 5s. for registering the notice, although some companies waive this and others charge less.

It is very desirable to get the age of the life assured admitted by the company, if the policy mentions that the age has not been admitted, for in the event of the age having been under-stated when the proposal was

made, the company would be able to deduct from the amount payable under the policy, the difference between the premiums that had been paid and those that ought to have been paid, with interest.

Before you can regard your security as perfected, you should inquire of the company if any prior dealings have been notified to them, to make sure, firstly, if there is any outstanding charge in front of you, and, secondly, that you have got with your security documentary evidence of any prior dealings and their discharge. If there have been earlier mortgages of the policy, you will require to file such mortgages, duly discharged, with the policy, for they form part of the chain of title and the company will require all such documents before paying over the policy moneys.

Occasionally you may be asked to lend money on a policy which you are informed has been lost. If you are satisfied as to the *bona fides* of your customer and that the facts are as he states, the only trouble you are likely to experience is getting the policy moneys from the company, which will require an indemnity before paying over.

But you must not forget that in such a case even if you protect yourself by giving notice and by ascertaining that no prior notices have been registered, circumstances may exist which will defeat your security. It was held in *Newman* v. *Newman* (1885), 28 Ch.D. 674, that an assignee having notice of a previous assignment which has not been notified to the company cannot get priority over such previous assignment by registering his notice forthwith.

Notice means not only actual notice, but constructive notice also. Thus, if you were asked to lend money against a lost policy, you might be held to be fixed with constructive notice that it was in a third party's hands by way of assignment, and so find yourself relegated to second place.

Equitable Mortgage. An equitable mortgage of a life

policy can be accomplished by the mere deposit of the policy with or without a memorandum of deposit. I imagine that rarely would a bank take a policy as a deliberate piece of security by such a method—the only cases occurring where you get hold of a customer's policy as a desperate remedy, on the understanding that it is to be held as cover for his debt.

The advantages of taking an equitable mortgage—cheapness and lack of formality—are decisively outweighed by the fact that you do not get a legal title and that, by the Policies of Assurance Act, 1867, companies are under no duty to recognise equitable interests. You will have to rope in the personal representatives if the policy becomes a claim, and you cannot surrender the policy during the assured's lifetime without his co-operation or the aid of the Court.

An equitable mortgage by deposit is good against a trustee in bankruptcy, for he is only an assignee by operation of law of the customer's interest in the policy, which interest will be subject to your equity acquired before the bankruptcy. But if you perforce have had to be content with the simple deposit of the policy, do not deal with it in any way that would suggest that you had waived your rights in it, such as by entering it in your safe custody records. In such a case a trustee might urge that the policy, having been lodged for safe custody and not for security, would have to be brought into the general estate.

If during the currency of an advance against the security of a life policy you receive notice of a second mortgage thereon, the account must at once be broken, so as to crystallise your rights against the security, unless, of course, by arrangement with the second mortgagee, you are allowed to let your customer range up to a named figure by way of fluctuating overdraft or otherwise.

Repayment of Advance. When an advance is repaid and the security is to be vacated, it will be necessary to put

the ownership of the policy back into the hands of the mortgagor. This is done, in the case of a legal mortgage, by sealing a formal reassignment, usually endorsed on the back of the mortgage form.

If the mortgage was to secure all moneys, the reassignment will have to be stamped at the rate of one shilling per cent on the highest amount advanced against the policy. If a limited charge has been used, stamping at this rate will be required on the limit inserted in the form.

The mortgage form, when endorsed with the reassignment, must on no account be cancelled or destroyed—it must be returned with the policy to the mortgagor, for it forms thenceforward part of his chain of title to the policy. It is, of course, necessary to acquaint the insurance company with your release of the policy, and this is usually done on a standard form.

Enforcement of Security. Finally, let us look at the formalities involved when it becomes necessary to enforce your security either because your customer is in default or, being the life assured, has died. If it is a case of a surrender, you must be careful to see that your power to deal with the policy has arisen—in some cases power is given in the mortgage form for surrender forthwith on default; in other cases, it is provided that a specified period of notice must be given of the bank's intention to surrender the policy.

But, in any case, it is the common practice to give a borrower the utmost latitude before depriving him of his equity in the policy, particularly because a life policy, as distinct from other types of security, has a potential value which should not be extinguished unless every possibility of dealing with the situation has been explored —such as getting a friend or a relative to buy the policy.

If it is necessary to surrender the policy, you should, first of all, find out from the particular company exactly what formalities are involved. It is usual to forward the mortgage deed as evidence of your claim, sometimes

accompanied by the policy itself. The company will draft a form of receipt, and this should be duly executed under the seal of the bank—although in a few cases, where policies of small amount are concerned, a receipt under the hand of the branch manager will be accepted.

If the receipt is endorsed on the policy, no receipt stamp will be necessary. The company will then issue its cheque for the surrender value on production of the policy, the form of mortgage (which will not require discharging), and the completed receipt.

If the policy becomes a claim by reason of the death of the life assured, proof of death will, of course, be required in addition to the above-mentioned documents, and in some cases proof of identity of the deceased will be called for.

CHAPTER IX

PAYMENT OF CHEQUES

"Banking companies should also, as far as it can be done with justice to others, give promotion to such of their servants as devote their leisure to the cultivation of their minds. The time is gone by when it was a reproach for a young man to be bookish, as he was supposed to abstract so much more time and attention from his official duties. It is now well known that the general cultivation of the intellectual powers renders them more effective in every operation in which they may be exercised.

"It is a great advantage to a public company to have educated servants. Their superior knowledge is always useful—the mental discipline they have acquired improves their business habits—and, possessing within themselves a constant source of enjoyment, they are the less likely to indulge in those expensive pleasures which are the usual temptation to neglect and dishonesty." —*Principles and Practice of Banking*, by J. W. Gilbart.

THE motive behind these worthy thoughts can scarcely be described as altruistic. There is the typical Victorian touch in the suggestion that, keep your clerks employed in improving their minds out of office hours, and they will not only prove better servants, but also will not cultivate profligate habits likely to lead to the robbing of tills.

I suggest that the need for knowledge, for mental discipline, is as urgent to-day as when the above extract was penned—but for a different reason. You should devote some portion of your spare time to the cultivation of banking knowledge, not because otherwise you may be led to use your leisure in doubtful pursuits and unwholesome pleasures, but because in these days,

in banking, as in other vocations, knowledge and that aptitude that flows from knowledge, are qualities the cultivation of which is necessary if our jobs—whatever they may be—are to be done effectively, with credit to ourselves and profit to those institutions which we are glad to serve.

We are not called upon to be legal experts or banking pundits. We cannot always regulate our banking business by legal precept and head office rules, but we should be equipped with that amount of knowledge which, fortified with a generous measure of common sense, will enable us to avoid the shoals of pedantry on the one hand and the rocks of ignorance on the other.

In considering the payment and collection of cheques, we shall be dealing with the root function of banking, for while no statutory definition of a banker exists that is worth calling a definition, competent authorities consider that the acid test of banking is the receipt of money, etc., from the public, and its repayment by cheque. Thus, whether you belong to the common-sense school, which believes that the everyday problems of banking can be decisively solved by the exercise of gumption and common sense, or to the textbook school, which likes to fit its daily work into the crabbed confines of theory, I imagine you will agree that a competent knowledge of banking practice, in relation to the payment and collection of cheques, forms the working tools of the average banker.

* * * *

The practice of bankers regarding the collection and payment of cheques is governed by what the law lays down on the subject—most of it being found in statutes and their interpretation by the Courts. Consequently, it is necessary to acquire some knowledge of the law in order to get a grasp of the practice.

Bills of Exchange Act. As you know, the principal statute is the Bills of Exchange Act, 1882—an example

of model draughtsmanship and orderly arrangement. This Act has some eleven sections specifically dealing with cheques as opposed to other types of bill, but let no one think that these sections sum up in its entirety the law relating to cheques, and that their assimilation will give one a grasp of all the legal implications involved.

A cheque is defined in Section 73 of the Act as a bill of exchange drawn on a banker payable on demand, and hence all references in the Act to bills payable on demand apply in like manner to cheques, with the one exception found in Section 45 (2). This provides that presentment of a demand bill must be made within a reasonable time after its issue or endorsement in order to render the drawer or endorser, respectively, liable.

In the case of a cheque, however, the drawer is liable on it for six years after its date, or the date of its issue, whichever is later, subject to the safeguard found in Section 74, which provides that a drawer of a cheque who suffers damage by its non-presentation within a reasonable time—as might happen if the drawee bank failed in the meanwhile—is discharged to the extent of such damage.

Not only are the sections dealing with bills on demand applicable to cheques, but so also are many other parts of the Act, such as those sections dealing with endorsement, presentment for payment, dishonour and notice thereof.

A right appreciation of the Bills of Exchange Act, an explanation of a good many of the provisos to numerous sections, and a proper idea of that party to a cheque whose rights are constantly safeguarded throughout the Act—that is, the holder in due course—can only be got by grasping the fact that a cheque is a negotiable instrument.

Negotiability. The time at our disposal does not permit of an exhaustive study of the doctrine of negotiability, but you should understand that there are three essential qualities attaching to a negotiable instrument.

Firstly, it must be such and in such a state that the

property in it—the legal ownership—can be transferred by mere delivery, accompanied, in the case of instruments payable to order, by endorsement. No instrument of transfer is required.

Secondly, it must give to a party who takes it honestly, for value, and without notice of any defect in the title of the transferor, an indefeasible title against all comers. So paramount is this quality of conferring a good title that a party taking a stolen negotiable instrument under the conditions just mentioned would have a good title against the party from whom it had been stolen.

Thirdly, a negotiable instrument must contain a right of action in itself; the possessor of it is deemed to be the true owner capable of enforcing any claims thereon—he is under no duty to justify his title in the first instance.

The party taking a negotiable instrument in the above circumstances is called a *bona fide* holder for value without notice, but in the case of a particular type of such instrument—a bill—the Act has designed a special term for such a party—holder in due course. And if in the course of your reading of the Act you wonder why there are so many provisos safeguarding this gentleman, the answer is that to preserve the scheme of negotiability it was necessary, when drafting the Act, to see that his remedies were not diminished nor his rights whittled away.

Now a cheque, being a bill, is ordinarily a negotiable instrument—the Act assumes that quality all the way through. This means that anyone taking a cheque under such conditions as to qualify as a holder in due course will acquire a complete title to the instrument, valid as against prior parties who have suffered by the transfer of the cheque, and enforceable against the party primarily liable on it—the drawer.

Many customers are of opinion that they have only to stop payment of a cheque in order to cancel the instrument. This is not so, for whatever may be the position between the drawer and the payee—such as false pretences or

fraud—which call for the countermand of payment, if the cheque gets outside the payee's hands, if it is transferred to a third party in such circumstances as to make him a holder in due course, such party can proceed against the drawer for the full value of the instrument.

He is not concerned with the disputes of what are called the immediate parties—the drawer and payee. He has acquired the cheque complete and regular on the face of it, honestly, for value, before it was overdue, without knowledge of any previous dishonour, or of any defect in the title of his transferor, and hence has every right to the property in the cheque. If you refer to Section 29 of the Act you will find that these are the requisites of a holder in due course.

If your customer wishes to make sure when he lets a cheque loose on the world that he will not be confronted by claims on it by outside parties, he should be told to adopt the remedy given him in the Act—to take the cheque out of the category of negotiable instruments by crossing it and adding in some proximity to the crossing the words "not negotiable."

Any party who thereafter acquires the cheque will not be able to derive a better title than any of his predecessors in ownership. If the payee's title to the instrument is affected with fraud, he cannot confer anything but a tainted title to his transferee, who will, consequently, not succeed against the drawer. He cannot be heard to complain, because he had a plain warning given him on the cheque in the shape of the "not negotiable" crossing, which was a clear intimation that he could not get or give a better title than previous holders possessed.

There are other ways by which a cheque can lose its negotiability. You remember that the holder in due course must take it before it is overdue. If he takes it in an overdue state he is taking something which is not a negotiable instrument.

Listen to what Section 36 (2) has to say—"When an overdue bill is negotiated, it can only be negotiated subject to any defect of title affecting it at its maturity, and thenceforward no person who takes it can acquire or give a better title than that which the person from whom he took it had."

In other words, you are back in the region of non-negotiability, and, after all, it is only reasonable that if you take an instrument which is manifestly stale, you are put on inquiry and should not be clothed with the rights of a holder in due course. Now, a time bill is overdue when its maturity date is past, but what of a bill payable on demand, such as a cheque?

The Act helps us to some extent in Section 36 (3), which says: "A bill payable on demand is deemed to be overdue within the meaning and for the purposes of this section when it appears on the face of it to have been in circulation for an unreasonable length of time. What is an unreasonable length of time for this purpose is a question of fact." You will see that the matter is to be decided by the facts of each particular case.

In a case reported on page 226 in *Legal Decisions*, Volume III, a County Court Judge held that a cheque dated twelve days previously was overdue when it was negotiated by a thief to a publican. In this instance the particular facts were that the thief had had the cheque in his possession for 13 days, notwithstanding that he told the publican he wanted money. The Judge held that the cheque was overdue when the publican cashed it. Hence as it was thus a non-negotiable instrument, he could only acquire the same right to it as the transferor—the thief—who had no title.

In an earlier case, *London and County Banking Company* v. *Groome* (1881), 8 Q.B.D. 288, it was held that the lapse of a period of eight days between the date of a cheque and its negotiation to a bank, though not conclusive, was a circumstance to be taken into account when

considering if the transaction ought to have aroused suspicion in the bank which exchanged the cheque. It is not possible to lay down a definite period of time at the end of which a cheque will be overdue; it is a question of fact in each case.

You must distinguish, however, between a cheque that is stale for the purposes of transfer and a cheque that is stale for the purposes of payment. The practice of bankers in returning cheques marked "out of date" if bearing a date some six to twelve months previously has no statutory warrant; it is a banking custom founded on the recognition of the banker's duty to look after his customer and to give him a chance of confirming, or otherwise, an instrument which by its nature should have been presented reasonably soon after its issue.

There is one final point to remember before we pass on. If the instrument is tainted with forgery of the drawer's or endorser's signature, no rights can be derived through or under the forged signature, and no party whose title rests on such signature can be a holder, let alone a holder in due course.

Banker and Customer. We will now proceed to consider some aspects of banking practice in regard to the payment of cheques.

Possibly the most concise and yet comprehensive outline of the mutual relations of banker and customer is found in Lord Atkin's summary in the appeal case of *Joachimson* v. *Swiss Bank Corporation*, [1921] 3 K.B. 110, where he says—

"The bank undertakes to receive money and to collect bills for its customer's account. The proceeds so received are not to be held in trust for the customer, but the bank borrows the proceeds and undertakes to repay them. The promise to repay is to repay at the branch of the bank where the account is kept and during banking hours. It includes a promise to repay any part of the amount due, against the written order of the customer addressed

to the bank at the branch, and, as such written orders may be outstanding in the ordinary course of business for two or three days, it is a term of the contract that the bank will not cease to do business with the customer except upon reasonable notice. The customer, on his part, undertakes to exercise reasonable care in executing his written orders, so as not to mislead the bank or to facilitate forgery.

"I think it is necessarily a term of such contract that the bank is not liable to pay the customer the full amount of his balance until he demands payment from the bank at the branch at which the current account is kept. Whether he must demand it in writing it is not necessary now to determine."

You get in this passage substantially the whole duty of the paying banker towards his customer, and you will notice that it enlarges the root relationship of debtor and creditor by recognising the agency function of the paying banker—his obligation not merely to repay his customer the amount of his credit balance, but also to honour his orders to pay third parties.

I propose to utilise the above passage as a framework on which to build the idea of the paying banker in practice, ignoring matters which, interesting though they may be from an academic standpoint, do not enter into practical considerations.

It will be seen that the rights and duties involved in this relationship are reciprocal. The banker's duties are the customer's rights, and, conversely, the customer is under certain duties to the banker—duties which are the latter's rights.

Banker's Duty to Pay. Now, firstly, the banker's primary contract is to repay moneys received for his customer's account, usually by honouring his cheque. You will remember that this cheque-paying function is the one which, according to the best authorities, is the distinguishing mark of a banker, the function that

differentiates him from other institutions which receive money from the public.

It follows from the exigencies of business that the banker's duty to obey his customer's mandate only extends to the branch where the account is kept, and a customer has no ground for complaint or action if his cheques are not honoured at branches elsewhere, unless he has made arrangements to this end. If such arrangements are made, the banker is under the same duty and possessed of the same rights as if the cheques were encashed at the parent branch.

You will find an opinion in *Questions on Banking Practice* (No. 488) to this effect, and, if correct, it means, among other things, that a banker will get protection against a forged endorsement on a cheque paid at another branch if he can come within the terms of Section 60. If, however, arrangements are made for the encashment of cheques at another *bank*, such protection will not be available to the latter, which, presumably, would expect the bank opening the credit to indemnify it against any loss so sustained, provided it had not been negligent.

Then the banker undertakes to repay in banking hours. You will find in Section 45 (3) that a bill—this, you remember, includes a cheque—must be presented for payment on a business day at a reasonable hour, and this is covered in the case of cheques by the phrase "banking hours." Incidentally, banking hours are fixed by custom, and not by statute, and if any departure is going to be made from established hours of business, due notice of such alteration must be given in the Press and by other means.

There is a dual danger in paying cheques other than to the drawer—that is merely a matter of expediency—presented out of banking hours. Firstly, if it transpired that you had paid a stolen cheque on which the endorsement was forged, you would be liable either to the true owner or to the drawer, for you would not have paid the

holder and hence would not have paid in due course, thus failing to obtain a good discharge as required by Section 59. In this instance, Section 60, which is designed to mitigate the rigour of Section 59 in so far as cheques are concerned, would not help you, for one of the conditions of protection under that section is that the payment shall be made in the ordinary course of business, and payment out of established hours is out of the ordinary course of business.

The second risk you would run would be that a customer might countermand payment of the cheque in question and bring evidence to show that it had been physically impossible for the article to have been presented within banking hours on the day he drew it. In such a case he might successfully resist being charged with the sum in question.

An interesting case bearing on this point is *Baines* v. *National Provincial Bank* (1927), 32 Com. Cas. 216, where a customer issued a cheque in circumstances which made it impossible for it to be presented in banking hours the same day. On requesting the bank to stop payment the next day, he found that the cheque had in fact been paid after closing hours on the day of issue.

It transpired in the action that, owing to the crowded state of the counter, due to market day, the cheque was paid at five minutes after the closing hour, and it was held that a bank is entitled to deal with a cheque within a reasonable business margin after its advertised time of closing, and in cashing the cheque the bank had acted within its rights and the action therefore failed. Thus, you are relieved from suspending business operations as the clock strikes the closing hour with that rigour which characterises a like hour on licensed premises.

Then the quotation from Lord Atkin goes on to say that the banker promises to repay any part of the amount due against the order of the customer.

Banker's Right to Set-off. Now, in computing the

amount due—the available balance—the question of set-off arises if the customer keeps more than one account in his own right. Of course, if one of the accounts is a trust account, known to the banker as such, or so earmarked as to constitute notice of trust, no set-off can be exercised over any credit balances on the trust account.

In this connection it is, perhaps, timely to remind you that, in the case of solicitors' accounts, you cannot exercise a right of set-off, by agreement or otherwise, over any credit balances on the "client" account or accounts that solicitors are now bound to keep. This is provided for by the Solicitors Act, 1933.

Apart from these considerations, the doctrine of set-off is one on which there is a good deal of conflict of opinion as regards the conditions under which it is exercisable. Is a banker entitled to set-off accounts in the same right *in the absence of agreement or course of business to the contrary*, or is such right of set-off dependent on an affirmative agreement by the customer to that effect? First of all, we must distinguish between a current or running account and a stopped account.

As regards the latter type, where an account is stopped by reason of death, bankruptcy, service of a garnishee order, etc., the banker's right of set-off is determined automatically. That is to say, before he accounts to the personal representatives of a deceased customer, to the trustee of a bankrupt customer, or to the High Court in respect of a garnished account, he is entitled to combine all accounts of his customer in the same right in order to get at the sum to be accounted for.

You will note that in all these cases no question arises as to risk of action by the customer for wrongful dishonour of cheques presented after set-off has been exercised. If the customer is dead, or bankrupt, no cheques will, in the ordinary course, come forward for payment; if they do, or if the account is garnished, any cheques presented

can safely be returned unpaid, quite apart from any question of available funds after set-off—such funds are to be accounted for elsewhere.

The question of set-off assumes a difficult aspect when unbroken current accounts are concerned, for the dishonour of cheques after the accounts have been combined is involved. The case usually quoted in the textbooks in support of the banker's right to combine current accounts in the absence of contrary agreement, is *Garnett* v. *McKewan* (1872), 27 L.T. 560.

The circumstances here were that the plaintiff in June, 1868, left the "B" branch of the London and County Banking Company with a dormant overdraft of £42 15s. 11d. In December, 1871, he opened another account at the "L" branch of the same bank, and by the end of the following month had thereon a credit balance of £42 18s. 10d. Three cheques were then presented amounting to £23 3s. and dishonoured, as the "L" branch had by that time become aware of the dormant debit balance at the "B" branch. The plaintiff was duly advised that this debit balance had now been liquidated by a transfer from his account at "L" branch.

From the law reports it does not appear that the special feature in the case—the dormant overdraft—was considered in the judgment, which was in the bank's favour, it being held that there was no special contract or usage proved to keep the accounts separate, and that while it might be proper and considerate to give notice to a customer of intention to combine accounts, there is no legal obligation on a bank to do so arising either from express contract or course of dealing.

A totally opposite view seems to have been taken in *Greenhalgh* v. *Union Bank of Manchester*, [1924] 2 K.B. 153. The Judge said: "If a banker agrees with his customer to open two or more accounts, he has not, in my opinion, without the assent of the customer, any right to move either assets or liabilities from the one account

to the other; the very basis of his agreement with his customer is that the two accounts shall be kept separate. . . ."

This case concerned the appropriation by the bank of the proceeds of matured bills, and in some quarters it is considered that the above remarks are not part of the binding judgment. Sir John Paget in the latest edition of his *Law of Banking* does not allude to the *Greenhalgh* case in this connection or vary his previously expressed views. He suggests that a banker can combine several accounts kept by a customer in his own right, unless by agreement, earmarking, course of business, etc., there is an obligation to keep them separate, "but," he says, "such combination should always be exercised with due care for the customer's credit and interests, the dishonour of outstanding cheques in particular being avoided if in any way possible."

In some quarters it is thought that the opening of two separate accounts by a customer is in itself an implied agreement to keep such accounts separate. In any case, I think I am interpreting banking practice aright when I say that it is now recognised that it would be inviting trouble arbitrarily to combine two accounts in a customer's name and to return a cheque drawn on a credit balance on one of them, unless you had given notice of your intention to set off or there was an agreement or established course of business to that effect.

There is a growing practice among banks to take a letter of set-off where a customer is borrowing on one or more accounts against credit balances on other accounts, such letter recognising the banker's right at all times to regard all the accounts as one. This seems a safe course to pursue in view of the conflicting opinions held as to whether, on the one hand, you have a right of set-off in the absence of agreement or course of business to the contrary, or whether, on the other hand, you have a right of set-off only if you have an agreement to that effect whereby the

customer waives his right to have the accounts kept separate.

I conceive that the merit of a letter of set-off is twofold —it is the best proof that your right of set-off exists, and it dispenses with the need for notice.

Uncleared Effects. In computing the available balance on your customer's account the question of uncleared effects must not be lost sight of.

It is not easy to pick one's way through the tangle of conflicting legal opinions as to the position of the banker who credits items paid in by his customer before proceeding to clear them, but I think the matter can be summed up from the practical point of view as follows.

Owing to the exigencies of business, bankers generally credit all articles paid in for collection to the particular customer's account forthwith. I imagine that the custom of delaying credit of country cheques until cleared has pretty well died out outside the City of London.

In some cases the items are described in the account and in the pass book as "Cash"; in other cases they are described as "Sundries." In *Capital and Counties Bank, Ltd.* v. *Gordon*, [1903] A.C. 240, it was said: "It must never be forgotten that the moment a banker places money to his customer's credit the customer is entitled to draw upon it unless something occurs to deprive him of that right."

This would suggest that the above system is a high price to pay for book-keeping convenience, inasmuch as it gives a customer an immediate right to draw against effects whose fate is unknown. But in the later case of *A. L. Underwood, Ltd.* v. *Barclays Bank*, [1924] 1 K.B. 775, it was said: "Though the cheques were in fact credited to the customer's account before they were cleared, the customer was not informed of this, and I can see nothing to prevent the bank from declining to honour a cheque if the payment in, against which it was drawn, had not been cleared." This appears to be in direct

conflict with the ruling in the *Gordon* case—a ruling of a higher Court—at any rate as regards items whose credit has not been communicated to the customer by pass-book or otherwise.

I venture to suggest in view of this disparity of legal opinion, that as regards credits uncommunicated to the customer, you can safely return cheques drawn against such credits, with the answer "Effects not cleared," because, among other reasons, no entry is binding on a banker until communicated to his customer. If, however, there is an agreement, either express or implied, such as would arise out of a course of business, to pay against uncleared effects, you would be bound to honour your customer's drawings regardless of whether the balance on his account was cleared or not.

An occasional latitude allowed your customer would possibly not be interpreted as course of business; but if, as with many of your customers, you regularly pay against uncleared effects, you cannot arbitrarily and without notice withdraw such facilities. But what of the case where a customer gets his pass-book showing uncleared cheques credited as "Cash"?

To cover such cases it is the habit of banks to caution customers, by means of a notice in the pass-book and elsewhere, to the effect that the bank reserves the right at its discretion, to postpone payment of cheques drawn against uncleared effects which may have been credited to the account.

The possibility of uncleared effects being included in a credit balance must not be overlooked when you are called upon to account to outside parties, as in the case of bankruptcy, notice of second mortgage, and service of a garnishee order.

In the last case you would be in order in transferring any uncleared items to a suspense account, provided you had not agreed to pay against them forthwith, for, although in *Jones* v. *Coventry*, [1909] 2 K.B. 1029, it was

held that items credited as cash were attached, notwithstanding that they were uncleared, the views expressed in the *Underwood* case mentioned just now are regarded by Sir John Paget as probably vindicating the course I suggest.

Countermand of Payment. Your contract to deal with your customer's balance according to his instructions, means that you must duly take note of any countermand of payment. I need hardly remind you of the necessity for getting such revocation of authority in writing and in unequivocal terms, for any confusion as to which cheque is the subject of countermand may possibly involve you in a twofold action—for paying a stopped cheque and for wrongfully dishonouring other cheques which, but for the payment of the stopped one, could have been honoured.

A case in point is *Hilton* v. *Westminster Bank, Ltd.* (1927), 43 T.L.R. 124, where a drawer countermanded payment of a cheque for £8 1s. 6d. by wire, the number being given as 117,283. This was later confirmed by telephone. A cheque for the same amount and similar details, save that the number was 117,285, was subsequently presented and paid, and it transpired that this was the cheque which it was intended to stop, its number having been given wrongly in the first instance.

The drawer sued the bank for having paid contrary to instructions and for having wrongfully dishonoured other cheques, which, but for such payment, could have been met. It was suggested that the bank officials were not entitled to assume that the cheque actually paid was a duplicate of the stopped cheque, for an examination of the paid vouchers would have shown that the cheque bearing the number given by the drawer had in fact been paid and did not correspond in detail with the stopped cheque.

Viscount Dunedin, giving judgment for the bank in the House of Lords, said: "It must always be remembered that a bank could be sued just as much for failing to

honour a cheque as for cashing a cheque that had been stopped. Under the regulations the bank had to inform the clearing house by 3.30 p.m. whether they honoured the cheque or not. They did not know the plaintiff's address, and when it came to a question of identification it must always be remembered that the number of a cheque was the one certain item of identification. There could be only one cheque bearing a printed number; there might be many cheques in the favour of the same payee and for the same amount.

"He was at one time inclined to think that, inasmuch as both the cashier and the manager knew that there was a stop on the cheque they ought, on 6th August, to have made certain investigations, but he found that they did do so. They followed the ordinary practice. They looked at the ledger and the ledger showed that no cheque in favour of the payee had come in. He thought, therefore, that the view of the officials was correct—that the cheque presented, being subsequent to the date of the stop instructions, might be a duplicate cheque and that they were bound to cash it."

Thus, make sure you get the number of the cheque when taking instructions for countermand of payment and no charge of negligence can subsequently be laid at your door.

A further point of importance is to see that you get prompt confirmation in writing of a stop given by telegram or telephone; not only is this a check on the details of the cheque, but you are not safe in acting on anything but written instructions.

In the case of *Curtice* v. *London City and Midland Bank Ltd.*, [1908] 1 K.B. 293, a customer stopped payment of a cheque by telegram which was delivered after office hours in the bank letter box. It was not noticed on the following morning when the box was cleared, and the cheque in question was paid before the telegram came to light. The Appeal Court held that there can be no

constructive countermand of payment, and that the cheque was not in fact stopped, as notification of such action did not actually come to the bank's notice.

There might have been a ground of action for negligence against the bank in respect of the careless clearing of the letter box, but the measure of damage would be by no means the same as in an action for money had and received. Thus the Court found in favour of the bank, and the case is particularly interesting inasmuch as a few words were said concerning the effectiveness of a telegraphic countermand of payment.

While a telegram, and presumably a telephone message, would justify a bank in postponing payment pending inquiry, it would not as a matter of law authorise the bank to refuse payment. Hence, you would be justified, when a cheque is presented which has been stopped by wire or telephone, in postponing payment or dishonour, pending corroboration, and any answer placed upon the cheque should make this clear.

One word about the answer to put upon a cheque that has been duly stopped. Not infrequently you see "Payment stopped," the use of which cannot be too strongly deprecated. It might suggest that the drawer is insolvent or in liquidation, or even that the drawee bank had suspended payment. The correct and proper answer is "Orders not to pay" or "Payment countermanded by drawer."

Garnished Accounts. The banker's contract to repay any part of the amount due to his customer is determined or conditioned by operation of law, or by the happening of such events as death or mental infirmity. I will deal briefly with some of these circumstances.

If a garnishee order, or summons, is served on you, the Court inhibits you for the time being from carrying out your undertaking to honour your customer's cheques drawn against funds in your hands. If circumstances make it expedient—as where you have a considerable

margin between the credit balance and the amount of the order—you may possibly elect to allow operations on a temporary account to which all payments-in subsequent to, and hence untouched by, the order will be placed.

The garnished account should not be operated upon, as that would be a defiance of the order of the Court. When contemplating the opening of a temporary account to be overdrawn on the strength of the credit balance on the stopped account, you should bear in mind that costs—which may be considerable if the issue is fought—are payable out of the sum in your hands, and that there is the possibility of the service of a second order or of bankruptcy intervening before the first order is discharged.

Of recent years, however, there has grown up a practice of stating in the order a specific sum (which includes probable costs) as the amount attachable, and in such a case you will, apparently, be safe in transferring the sum so stated to a suspense account pending settlement of the order, and in allowing operations to continue on the main account. I cannot find any authority for this practice of varying the rules of the High Court, which provide that the whole balance is attached, but I suggest that you run little or no risk in interpreting literally the modern type of limited order which ordains that "all debts owing or accruing due not exceeding £...................... be attached," etc.

Bankruptcy of Drawer. Another case when your contract to pay is overruled by operation of law is when your customer becomes involved in bankruptcy proceedings: we will take matters in the sequence in which they appear in the Bankruptcy Act.

First of all, if your customer has committed an act of bankruptcy, your authority to pay his cheque is cut down to payments to himself—third party cheques must be returned with the answer "Refer to Drawer." It will be necessary, before taking this drastic step, to satisfy

yourself, of course, that one of the eight statutory acts of bankruptcy has been committed. This is not always an easy matter to decide, particularly as possibly the most common of these acts is where a customer gives notice of suspension of payment of his debts. Such notice need not be in writing, and consequently you may have to decide whether what you have heard from other parties was gossip or a repetition of what your customer had stated to them.

Usually a debtor calls a meeting of his creditors to announce this initial step towards the Bankruptcy Court, but notice of the calling of a meeting of creditors is not in itself an act of bankruptcy, and unless you are positive that your customer has categorically announced in writing or otherwise, that he is suspending payment, you will not be safe in dishonouring his cheques payable to third parties. You should take an early opportunity of ascertaining what took place at the meeting and shape your course accordingly. Furthermore, a debtor may at the meeting of creditors admit insolvency, but that by itself will not constitute an act of bankruptcy.

The case of *Anglo-South American Bank* v. *Urban District Council of Withernsea* (1925) is illuminating on this point.

A debtor had attended a meeting of his creditors and admitted that he was insolvent. He definitely refused to file his petition, however, and declared his intention of carrying on business until he was compelled to stop.

The judge held that no act of bankruptcy had been committed and laid down three useful precepts to follow in deciding this nice point.

Firstly, the bankrupt's statement must be more than a mere casual remark—it must be a statement that by its form appears to be an intentional statement by the bankrupt of something that he has already done or something he intends to do.

Secondly, a statement by or on behalf of a debtor that

he is insolvent, whether the deficiency be great or small, is not of itself an act of bankruptcy unless, indeed, it amounts to a statement of inability to pay each and every one of his creditors.

Thirdly, a statement of insolvency may be made on such an occasion and with such surrounding circumstances that a reasonably minded creditor would understand it as an intimation that the debtor had suspended, or was about to suspend, payment of his debts generally, and if it be so made it is an act of bankruptcy.

It is for you, therefore, to consider if the reasonable inference from a debtor's remarks is that he has suspended or is on the point of suspending payment of his debts.

Now what would happen in practice? I imagine that if you were in a quandary as regards paying your customer's cheques on these grounds, you would get into touch with him or his accountant, or his solicitor, to ascertain the facts and base your action on what you were told. But usually when confronted with a cheque in circumstances which leave you in doubt as to whether an act of bankruptcy has been committed, you cannot get hold of your customer, or his accountant, or his solicitor. In all such cases of indecision a sound rule to adopt is to act in such a way as will fix your possible liability.

In the case in question, if you pay the cheque and it transpires that an act of bankruptcy has taken place, your loss will be the amount of the cheque, which you will have to refund to your customer's trustee, whose title will relate back to the date of the commission of the act. If, however, you dishonour the cheque and it transpires that your customer's conduct or statement did not amount to an act of bankruptcy, your loss will be the amount of damages which he can get out of you for wrongfully dishonouring his cheque. But you may say—suppose the cheque is of large amount, what then? In such a case, try to arrange with the presenting banker for a little grace, or put the onus of decision on your head office.

The next step in bankruptcy is the presentation of a petition, and if you have notice of such an event, you must pay no more cheques to your customer or to third parties.

Lastly, if a receiving order has been made, its effect is to stop all operations on the account as from the first moment of the day it is made. You should remark that it is not notice of a receiving order, but the making of it which *is the crucial point of time.*

Sometimes the first intimation you get is a notice in *The London Gazette*; sometimes it is a communication from the Official Receiver; but all cheques paid on or after the day the order is made are money thrown away unless you can come within the very limited protection of Section 4 of the Bankruptcy (Amendment) Act, 1926. This provides that if you have paid away any of the debtor's balance on or after the date of the receiving order, in ignorance of it and before it has been gazetted, the trustee must, if practicable, recover the moneys so paid from the payee of the cheque. This covers the occasional case where advertisement of a receiving order is postponed and you do not hear of it from other sources, but apparently if there is any difficulty about proceeding against the payee, the trustee can still call on you to refund the sum in question.

Dishonour of Cheques. If for any reason you are under the necessity of returning a cheque drawn on you, there is nothing statutory that makes it compulsory for you to give a written answer thereon. In the case of cheques presented through the London Clearing House, however, no unpaids will be received back without a written answer—this is by virtue of the Clearing House Rules, which state "No return can be received without an answer in writing on the return why payment is refused."

While at times it might be useful to return a cheque presented through non-clearing channels without committing yourself to a written answer, such a course is

fraught with risks. Apart from the fact that the presenter would assume the worst about your customer, you may be aiding the fraudulent negotiation of the cheque to the drawer's detriment. For if a cheque bears a written reason for its dishonour on its face, no person who subsequently acquires it as a holder can get the rights of a holder in due course against the drawer, for one of the requisites of a holder in due course, as mentioned earlier, is that he shall take the instrument "without notice that it had been previously dishonoured if such was the fact."

When under the necessity of returning a cheque, whether on account of a legal bar to payment, for want of funds, or for some technical irregularity, a banker must take particular care not to damage his customer by an unwarrantable answer.

First of all, let me remind you that whatever answer you elect to put on an unpaid cheque must be written in full if you are returning it under the rules of the London Clearing House—and I imagine that through whatever channel the cheque has been presented, it is now the practice to give an unabbreviated answer. So you are no longer perplexed by such conundrums as "N.P.F.," "E.N.C.," "N/S," which were the attenuated symbols of "Not provided for," "Effects not cleared," and "Not sufficient funds," respectively.

Then make it a rule to put on the answer which really fits the case, eschewing such euphemisms, for example, as "Exceeds arrangements," which is revealing more than you are justified in doing, as it plainly announces that your customer is taking accommodation from you and happens to have overshot the mark. If you are returning a cheque for want of funds, the fit and proper answer is "Refer to Drawer," and if you wish to insinuate that hope need not be entirely abandoned you can add "Present again," without suggesting a date, however.

Then remember that "Refer to Drawer" is an answer not confined to cases of dishonour for want of funds. It

is, for example, the correct answer on a cheque that is being returned by reason of the garnishing of the account, or because your customer is involved in bankruptcy proceedings. On the other hand, discretion should be exercised in applying it in other instances. It is true that the words themselves are innocuous and merely invite the presenter of the cheque to inquire of the drawer as to the reason for dishonour, as was suggested in the case of *Flach* v. *London and South Western Bank, Ltd.* (1915), 31 T.L.R. 334. They have, however, acquired a particular if erroneous meaning to the man in the street, namely, that there are no funds on the drawer's account.

In the case of *Frost* v. *London Joint Stock Bank, Ltd.* (1906), 22 T.L.R. 760, where, by the way, the circumstances were unusual and peculiar, the Court of Appeal laid down certain principles as to what would constitute a libellous answer on a cheque, and held that where words are not plainly and solely defamatory in their meaning the test is not what they would convey to a particular class of person, but what they would suggest to a reasonable person of average intelligence. Nevertheless, I think you will agree that to avoid risk of an action for libel, "Refer to Drawer" should only be used where there are no funds on the drawer's account, or where by his own action he has put you in the position where you are prevented from parting with his balance by operation of law.

I suggest this in face of the dictum of Lord Shaw, in *London Joint Stock Bank, Ltd.* v. *Macmillan and Arthur*, [1918] A.C. 777, viz., "If there be on the face of the cheque any reasonable ground for suspecting that it has been tampered with, then that in the usual case is met by the marking 'Refer to Drawer,' and by a delay in payment until that reference clears away the doubt."

"Not Negotiable" Crossing, and "Account Payee." Cheques crossed "not negotiable" or "Account payee" which come forward for payment bearing endorsements evidencing transfer, are sometimes regarded as awkward

documents to deal with. Some people think that the words "not negotiable" are inconsistent with the outward and visible signs of transfer in the shape of a string of endorsements on the back of a cheque.

But to hark back to first principles—"not negotiable" does not mean "not transferable," the term is not addressed to the paying banker, but to successive holders of the cheque, and it warns them that they had better pay regard to what they know of the transferor, for they cannot get a better title than he happens to have. A cheque so marked can be freely transferred, but is no longer free from the equities or rights of other people. Hence, a paying banker is not concerned with the phrase, quite apart from the fact that it may not have been put on by the only person to whom he is responsible—the drawer.

Then with regard to the "Account payee" crossing, a paying banker is likewise under no duty to take heed of the phrase. It has no place in the Bills of Exchange Act; it is an unauthorised addition to the cheque that is only indirectly recognised by the Courts in that, as we shall see, disregard of it by a collecting banker will be accounted to him as negligence.

The paying banker is under no duty to see that the proceeds of a cheque so marked are applied as directed, for firstly, the words may have been added by the payee and the banker is only concerned with his customer's instructions, apart from those additions in the shape of crossings permissible to third parties. Secondly, even if the drawer issued the cheque so marked, the banker is entitled to ignore this unauthorised addition; he can say that his customer has issued an ambiguous document, in that he has inserted words on the cheque that are inconsistent with the machinery of tranfer indicated by the words "or order," and that he is entitled to rely on the legal form of the cheque and to disregard unauthorised and ambiguous additions.

These considerations equally apply where a cheque bears evidence, in the shape of additional endorsements, that it has not gone to the account of the payee. The only possible risk would arise where one of the endorsements was forged, when the customer might complain that the cheque was not paid in the ordinary course of business under Section 60, or without negligence under Section 80; or the true owner might sue for conversion. As against this, Sir John Paget is of the opinion that the Courts would hold that the words "A/c payee" are addressed to the collecting banker, and in no case have any significance for the paying banker.

Occasionally a cheque comes forward drawn "Pay A.B. only," or "Pay A.B. not transferable," with the words "or order" or "or bearer" duly deleted. This is an embarrassing form of cheque, but, unfortunately, it has legal warrant, for Section 8 of the Bills of Exchange Act contemplates this sort of instrument when it says: "Where a bill contains words prohibiting transfer, or indicating an intention that it should not be transferable, it is valid as between the parties thereto, but is not negotiable." If an open cheque so marked were presented for payment, you would have to identify the payee beyond all doubt, and if such a cheque were presented through the Clearing, the presence of endorsements additional to that of the payee would necessitate your returning it.

Forgery. It necessarily follows from the banker's contract to repay his customer's money against his written orders, that if he perchance pays away funds against a forged order, he cannot charge such sum to his customer's account. There seems to be an impression in some people's minds that the banker will lose on account of negligence. As a matter of fact, negligence has nothing to do with the matter, and in a good many cases the signature has been so cleverly forged that a customer could not set up want of care on the banker's part. The

reason why, in the ordinary course, a banker cannot debit his customer with a forged cheque is that he has broken his contract—he has not paid against his customer's genuine order.

The circumstances in which a banker may be able to debit his customer with the amount of a forged cheque are where the customer adopts the signature as his own, or where the doctrine of estoppel can be invoked against the customer. A pure and simple forgery, as opposed to an unauthorised signature, cannot be ratified, as ratification presupposes agency that has been exceeded or abused. It can be adopted, however—that is to say, the customer may state: "I will treat this signature as my own and you may charge me with this cheque."

Alternatively, a customer, by his conduct, may be prevented or estopped from denying the genuineness of the signature in dispute. Where, for example, the drawer knows of the wrongful use that is being made of his cheques and does not warn the bank, it is conceivable that he could not successfully set up the forgery, for his own conduct had led the bank into paying the forgeries.

Lord Justice Scrutton, in *Greenwood* v. *Martins Bank Ltd.*, [1932] 1 K.B. 371, when mentioning the duty of a banker to report to his customer an attempt to cash a forged cheque, emphasised the corresponding duty of the customer to warn his banker of the existence of any such cheques.

> "The banker, if a cheque were presented to him which he rejected as forged, would be under a duty to report that to the customer to enable him to enquire into and protect himself against the circumstances of the forgery. That would involve a corresponding duty on the customer, if he became aware that forged cheques were being presented, to inform the banker in order that the banker might avoid loss in the future."

The above-mentioned case concerned a customer, who, after his wife had confessed to forging his cheques, held

his peace, and only disputed the state of his account after his wife's untimely death.

It was held in the Appeal Court that the customer was estopped from setting up the forgeries, not because his silence led the bank into loss—for the cheques in question had all been paid before he was made aware of his wife's delinquency—but because his silence had prevented the bank bringing a civil action against the forger, which might have had good, if curious, results, as at that time the husband would have been liable for his wife's tort.*

So much for the forgery of a drawer's signature, but there are other matters than the regularity of the drawer's signature that have to be considered. For example, in paying a cheque a banker must get a good discharge for his customer, and reference to the Bills of Exchange Act, 1882, Section 59, will show that a bill (or cheque) is discharged by payment in due course, which means payment to the holder of the cheque in good faith and in ignorance of any defect in such holder's title. Sir John Paget referred, in the Gilbart Lectures in 1916, to the situation envisaged by the late Lord Halsbury, of a decrepit and seedy looking individual presenting an open cheque for a large sum payable to bearer. Would payment to such a person be payment in due course? Lord Halsbury inclined to the view that a banker would hesitate very much before paying such a cheque, and I believe that in practice open cheques presented by strangers are the subject of special scrutiny and that attempt is made to delay payment if there is any suspicion as to the presenter's title.

You must not forget two things, however—if you refuse or delay payment without justifiable cause, your customer may have a cause of action; the holder of the cheque, of course, cannot take proceedings against you, because there is no contractual relationship between you and him.

* By the Law Reform (Married Women and Tortfeasors) Act, 1935, a husband is no longer liable for his wife's torts.

Secondly, if you make a habit of querying the *bona fides* of a stranger presenting a cheque, you are going to bring such a practice into the ordinary course of business and make a rod for your own backs on other occasions.

A case in point is the encashment of open cheques payable to a limited company, and purporting to be duly endorsed on behalf of the company. In view of the fact that it is rare for a company to do otherwise with cheques payable to itself than to pay them to its account, there is a natural hesitancy on the part of cashiers to pay a cheque in favour of a limited company over the counter to a stranger, and in some cases endeavour is made to get into touch with the company concerned by telephone if the presenter cannot produce the company's authority to deal with the cheque. You are under no duty, however, to the payee—the company—and it may be that the prompt payment of the cheque is an urgent matter for your customer, who will have something to say if you hesitate in obeying his mandate.

You are paying in due course under Section 59, as long as you have no notice of the holder's lack of title, and it would have to be something so patent as to arouse suspicion in a reasonable person's mind—constructive notice has no place where negotiable instruments are concerned. Furthermore, you are not concerned with the genuineness of an endorsement correct in form if the protective elements of Section 60 are present.

If any let or hindrance is to be placed on the encashment of open cheques, the distinction between open and crossed cheques will disappear.

A person claiming under a forged endorsement cannot be a holder, and hence, as far as Section 59 is concerned, you have not paid in due course, and thus have not got a good discharge if you pay a cheque bearing a forged endorsement.

Inasmuch as it is the exception for a banker to know an endorser's signature on a cheque presented for payment,

he would find the business of paying cheques to unknown holders decidedly unhealthy if Section 59 were the last word on the subject. In recognition of this fact relief is given to a banker by Section 60 in respect of the payment of cheques with forged or unauthorised endorsements—you must remember that an unauthorised signature is just as nullifying as a forged signature unless ratified.

But certain conditions have to be fulfilled to come within the protection of Section 60. It speaks of a bill to order on demand drawn on a banker—that you will recognise as a cheque—bills other than cheques bring the banker no protection; analogous documents to cheques such as conditional orders are not within its ambit and protection must be looked for elsewhere for such instruments. Then the banker must act in good faith—that is honestly—and in the ordinary course of business.

Ordinary Course of Business. This last is a phrase which, like the term "negligence," is unsatisfactorily elastic, and in fact very little guidance in the shape of decided cases or otherwise is available. Certain it is that payment of a cheque out of business hours is not in the ordinary course of business, neither is the payment of a crossed cheque over the counter to a non-banker.

Nothing is said in Section 60 about acting without negligence, and presumably you can be as careless as you please, but provided such carelessness is not so gross as to impugn your good faith, you are not put outside the pale of Section 60.

Of course, the forged endorsement must purport to be correct in form, and you would not get any help from the section if there was a manifest irregularity in the spelling or form of endorsement, for it is not in the ordinary course of business to pay cheques so endorsed.

There is another section that may save you if you pay against a forged endorsement—it is restricted to crossed cheques—and that is Section 80. This section requires the banker to act in good faith—honestly—but while it has

nothing to say about ordinary course of business, it requires the banker to act without negligence. I do not think that a paying banker can regard Sections 60 and 80 as alternative protections, in that if he is debarred by his conduct from setting up the one, he may be able to profit by the other. Section 60 deals with cheques bearing forged or unauthorised endorsements; Section 80 deals with crossed cheques only, and covers order cheques with forged or unauthorised endorsements and also bearer cheques. If you were unable to set up Section 60 because you acted out of the ordinary course of business, you would likewise be unable to plead Section 80, because to act out of the ordinary course of business would be negligence.

A case in point is *Slingsby and Others* v. *District Bank Ltd.*, [1932] 1 K.B. 544, where a cheque payable to "John Prust and Co. per Cumberbirch and Potts" was paid by the drawee bank bearing the endorsement "Cumberbirch and Potts." It was recognised by the court that this endorsement was wrong in form, the correct endorsement being "John Prust and Co. per Cumberbirch and Potts" or some form indicating agency. Inasmuch as this irregular endorsement was unauthorised, the bank was liable because Section 60 only protected against unauthorised endorsements that were correct in form—it was out of the ordinary course of business to pay against an incorrect endorsement. Likewise Section 80 was of no avail, for to pay on an incorrect endorsement was to be precluded from setting up the defence of acting without negligence. We shall find presently that there was another count on which the bank was liable in this case.

We have seen that a banker is under manifold duties to his customer as regards paying away the latter's funds; the customer, likewise, when drawing up his mandates for the payment of moneys in his banker's hands, is under a duty to his banker.

Customer's Responsibility as Drawer. He must take

care that he draws his cheques in such a fashion that he does not mislead the banker, that no loopholes are left for fraudulent manipulation by outside parties; in other words, the banker has a right to have cheques drawn on him in an unambiguous and unequivocal manner.

The House of Lords made this abundantly clear in the case of *London Joint Stock Bank Ltd.* v. *Macmillan and Arthur*, [1918] A.C. 777, where Lord Finlay said—

> "It is beyond dispute that the customer is bound to exercise reasonable care in drawing the cheque to prevent the banker being misled. If he draws the cheque in a manner which facilitates fraud, he is guilty of a breach of duty as between himself and the banker, and he will be responsible to the banker for any loss sustained by the banker as a natural and direct consequence of this breach of duty."

Viscount Haldane was to the same effect—

> "The customer contracts reciprocally that in drawing his cheques he will draw them in such a form as will enable the banker to fulfil his obligations and, therefore, in a form which is clear and free from ambiguity. The banker, as a mandatory, has a right to insist on having his mandate in a form which does not leave room for misgiving as to what he is called upon to do."

The cases where these matters become important are where a material alteration has been made to a cheque. Section 64 says that where a material alteration has been made to a bill without the assent of all parties liable on it, the bill is avoided. Thus, if a cheque is altered after it leaves the drawer's hands, without his permission (apart from additions permitted by statute, such as a crossing, etc.), he can disown it, and if the banker pays it he cannot charge the drawer. This general proposition requires modification, however, in the light of what I have just said.

If the alteration is apparent, then the banker who pays the cheque will, of course, have to stand any loss; so will he if the alteration is non-apparent, provided that the drawer used due care in drawing the document. But if the alteration is non-apparent and it can be shown that the drawer, by his carelessness in drawing the cheque, made it possible for the cheque to be tampered with, he will have to suffer the loss.

It is a case of two innocent parties suffering loss at the hands of a third party, and the rule of law is "that wherever one of two innocent persons must suffer by the act of a third, he who has enabled such third person to occasion the loss must sustain it" (*Lickbarrow* v. *Mason* (1787), 6 East. 20).

In the *Macmillan* case from which I have just quoted, a confidential clerk in the employ of a firm obtained the signature of one of the partners to a petty cash cheque whereon no amount in words was inserted, but the figures 2. 0. 0. were written in the appropriate space. The partner signed the cheque in this inchoate state and the fraudulent clerk thereafter inserted the figure "1" in front of the figure "2" and "0" after it, added in the proper space "One hundred and twenty pounds" in words, presented the cheque at the firm's bankers, obtained the money, and bolted.

The bank was sued by the firm for £118, being the difference between the amount of the cheque as drawn and as paid.

The lower Courts found for the firm, but the House of Lords reversed their decision and established the principle that if a customer is careless in the manner in which he draws a cheque, and any subsequent fraudulent dealing with the cheque is made directly possible by such want of care, then the customer and not the bank must bear the loss. They approved what was said in *Lewes Sanitary Steam Laundry Co.* v. *Barclay, Bevan and Co., Ltd.* (1906), 11 Com. Cas. 255, regarding a customer's obligation "to

be careful not to facilitate any fraud which, when it has been perpetrated is seen to have in fact flowed in natural and uninterrupted sequence from the negligent act."

It must be remembered that any unauthorised material alteration of a cheque is a species of forgery, whether it be "raising" the amount thereof or altering the tenor of the instrument in any other way. If a banker pays a cheque so altered, he, in the absence of contributory negligence, as in the *Macmillan* case, is in very much the same position as if he had paid a cheque whereon the drawer's signature was forged.

The case of *Slingsby* v. *District Bank, Ltd.*, mentioned previously, is an illustration of the risks a banker runs in this connection, risks which in some cases cannot be guarded against as the alteration is non-apparent. In the case in question a solicitor acting for a body of executors prepared a cheque payable to John Prust and Co.—a firm of stockbrokers—for £5000 and sent it to the four executors for their signatures. On receiving it back duly signed, he added after the payee's name—sufficient space being available—the words "per Cumberbirch and Potts"—the name of his firm.

Now the cheque on the face of it was a perfectly regular instrument; it was in one handwriting save for the drawers' signatures, and the bank paid it on presentation. The cheque having been misappropriated by the solicitor, the executors sued the drawee bank, having been unsuccessful in an earlier action against the bank that collected the cheque for an account in which the fraudulent solicitor was interested.

In the lower Court it was held that, apart from the irregularity of the endorsement to which I made reference, the bank was liable in that it had paid a forged instrument in the shape of a materially altered cheque. It was suggested for the bank that the leaving of a space to the right of the payee's name, thus facilitating the unauthorised insertion of "per Cumberbirch and Potts"

was an act of carelessness on the part of the drawers, comparable to the negligence of the partner in the *Macmillan* case.

The Judge held that the leaving of such a space was not unusual, no one could reasonably be expected to anticipate such an alteration, and there was no breach of duty on the drawer's part. This verdict was upheld in the Appeal Court, but Lord Justice Scrutton, while satisfied that it was not a usual precaution to draw lines before or after the name of the payee, significantly hinted that if such happenings became frequent it might become a usual precaution.

Closing a Customer's Account. Lord Atkin's summary of the relationship between banker and customer lays it down that a banker must give a customer reasonable notice of his intention to close the account, on the grounds that the customer's cheques may be outstanding for two or three days, and hence time must be allowed for their presentment.

There are two cases bearing on this point. In *Buckingham* v. *London and Midland Bank* (1895), 12 T.L.R. 70, the bank amalgamated the customer's loan and current accounts consequent on the latter giving a second mortgage on the security which the bank considered was overvalued in its books. The customer was told that his account was closed, despite his protests that cheques and bills were outstanding, and these instruments were in fact dishonoured when presented.

The jury found that the course of business with the customer was to let the current account work independently of the loan account, and that reasonable notice of the discontinuance of such course of business was required and was in fact not given.

In *Prosperity, Ltd.* v. *Lloyds Bank, Ltd.* (1923), 39 T.L.R. 372, the bank gave its customer one month's notice to close its account, and an injunction was thereupon sought to restrain the bank from such action on the ground

that the company's ramifications were such that one month's notice was not sufficient.

The Judge held that in the circumstances the prescribed notice was insufficient. He laid it down that a banker had the right to close a debit account at any time—presumably on the assumption that all banker's advances are repayable on demand—but in the case of a credit account, reasonable notice must be given, which would vary according to the facts of each case.

You will note that the doctrine enunciated in the latter case is an advance on Lord Atkin's statement of the position which only contemplated a sufficient period of notice to deal with outstanding commitments, as was the issue in the earlier case of *Buckingham* v. *London and Midland Bank, Ltd., supra.*

If you have an undesirable and obstinate customer who will not close his account after the expiration of reasonable notice, the only steps you can take are to ensure that no more credits are received, and to await the exhaustion of his stock of cheque forms. To send him his balance by registered post is a course not to be recommended, as outstanding cheques may come forward for payment subsequently, which, if returned, might involve you in an action for wrongful dishonour.

Receipts on Cheques. There is an increasing practice for business customers to embody a form of receipt in their cheques; in some cases it is merely stated that such receipt serves as an endorsement, in other cases there is a direction to the banker that the receipt must be duly completed before payment is made.

In the first case the unconditional quality of the document is unimpaired and it is, therefore, technically a cheque. But as a signature cannot serve the dual function of a receipt and an endorsement, it is customary to require customers who use such cheques to give an indemnity to the drawee banker, providing that he shall be in the same position as regards protection under Section 60, or

Section 80, as if the instrument were in fact endorsed and not merely receipted.

You must not forget that it is not only the drawer who could query the payment of a cheque with the payee's signature forged. The true owner could have a claim against you for conversion, and thus the indemnity must not only preclude the drawer from objecting to being debited with a cheque with a forged discharge, but must also make him liable to reimburse you if the true owner succeeds against you in an action for conversion. It thus follows that such indemnities are only of use if your customer is a man of substance.

As regards the second class of instrument which, by reason of the condition embodied therein, is outside the category of cheques, and therefore not within the protection afforded by Section 60 or Section 80 of the Bills of Exchange Act, some measure of relief is given to the drawee banker by Section 17 of the Revenue Act, 1883. This, in short, provides that Sections 76 to 82 of the Bills of Exchange Act, 1882, shall apply to such documents, which, however, remain non-transferable instruments.

This means that such documents must be crossed, for the sections referred to are the crossed cheque sections of the Act, and further, that they must show no evidence of having gone outside the payee's hands. Thus, the presence of a further endorsement would presumably deprive a paying banker of any protection.

In practice, bankers prefer not to rest on this section of the Revenue Act for protection, but take an indemnity which puts them in the same position as if they had paid a cheque.

In paying banker's drafts—that is, drafts drawn by one branch on head office, or on another branch—you are protected against forged endorsements by Section 19 of the Stamp Act, 1853, in the case of uncrossed drafts, and by the Bills of Exchange Act (1882) Amendment Act, 1932, in the case of crossed drafts. This amending Act

applies the provisions of the principal Act as regards crossed cheques (Sections 76-82) to banker's drafts, which can now be effectively crossed.

Payment of Domiciled Bills. In paying bills other than cheques the banker derives no protection against forged endorsements from the Bills of Exchange Act or from any other enactment.

Inasmuch as a banker at whose office a bill is domiciled is ordinarily not in a position to check the genuineness of an endorsement, this means that a certain amount of risk is run in undertaking to pay customers' acceptances.

Apart from taking an indemnity from a customer to cover the risk, the banker's only remedy is to adopt the suggestion once made by a judge—request his customer to domicile his acceptances at his business address.

While, possibly, this is not a course likely to be adopted, it must be remembered that the payment of bills is not part of the banker's essential contract with his customer, and in the absence of special arrangements, a customer has no right to accept bills payable at his bankers. Apart from the risk of forged endorsements, a banker paying an acceptance is safe, provided he pays the bill in due course according to Section 59. This means paying without knowledge of any defect in the title of the holder.

The case of *Auchteroni and Co.* v. *Midland Bank Ltd.*, [1928] 2 K.B. 294, is interesting on this point. This firm handed a matured bill, domiciled at the Midland Bank, to their cashier for the purpose of payment into their bank account for collection and credit. The cashier, in fraud of his employers, himself presented the bill at the Midland Bank, obtained the proceeds and bolted.

Auchteroni and Co. sued the bank for the amount of the bill, alleging negligence and conversion. The charge of negligence failed as there was no privity of contract between the parties; the Midland Bank was under no duty to the plaintiffs.

As regards conversion, the bill had been properly

discharged, the requirements of payment in due course under Section 59 having been duly carried out. There were no suspicious circumstances suggestive of lack of title in the presentation of the bill. The judge suggested that if a bill were presented by an office boy, or a tramp, inquiries would be indicated—thus getting back to Lord Halsbury's views mentioned previously.

If you say, what is the degree of respectability below which inquiries are requisite, I think the test the Courts would apply would be that of reasonableness—would the circumstances of presentation of the bill arouse suspicion in the mind of a reasonable man of ordinary intelligence ?

I think you will all agree that the position and responsibilities of the paying banker are fairly well defined in relation to his customer; there are, of course, risks inherent in his function as agent for his customer, just as there are risks in other businesses. You will no doubt admit, however, that the paying banker has received a reasonable amount of protection in the shape of Section 60 and Section 80, and also in the recognition by the Courts that the drawer of a cheque, while enjoying certain rights, is under a corresponding duty to be careful in framing his orders on his banker.

10—(L.2) 24pp.

CHAPTER X

COLLECTION OF CHEQUES

WHEN we come to consider the position of the collecting banker we find that there is no finality about his responsibilities; there is no certainty that what may be judicially regarded as normal to-day may not be branded as irregular to-morrow. The people to whom he is accountable are not merely his customers, but a great army of true owners with whom he has ordinarily no contractual relationship.

The past few years have seen a tightening up of office regulations, an outpouring of warning circulars, a whittling away of the recognition that a cheque is a transferable and negotiable instrument, in a desperate attempt to make harder the lot of the evil-doer who uses the bank as the medium for collecting stolen cheques.

While it is well that we should all be made aware of the dangers that beset a receiving cashier, it must not be overlooked that this steady stream of domestic instructions is encompassing us about with a great cloud of hostile witnesses, as was evidenced in the case of *Savory and Co.* v. *Lloyds Bank Ltd.*, [1932] 2 K.B. 122. In the House of Lords' hearing of this case it was recognised that although a bank's internal rules might fall short of or exceed what the Court might consider to be a bank's bounden duty, yet they afford a valuable criterion of the risks of which a bank is particularly aware.

The first step in our study of banking practice regarding the collection of cheques is to distinguish between the banker who acts simply and solely as an agent for his customer, acquiring no interest in the cheque, and the banker who in one way or another becomes a holder for value, and possibly a holder in due course, of cheques he

handles—cheques which he collects for himself and not for his customer.

This is no academic distinction, and you will appreciate that in some cases a banker will find it advantageous to set up as a holder for value, or, better still, as a holder in due course. Thus, where the transaction has been tinged with negligence so that there is not the protecting cloak of Section 82 of the Bills of Exchange Act, 1882, there is hope if you can show that you have not acted as an agent but as a holder for value of the cheque, for negligence is then immaterial.

Conversely, there may be circumstances where it will profit you to set up a defence under Section 82 as an agent for collection; for example, where there is a forged endorsement on the cheque. For provided the protective elements of Section 82 are present, a forged endorsement is immaterial. The presence of such a forgery, however, would be fatal to a defence of holder in due course, because there can be no legal holder under a forged signature.

The existence of this alternative defence has been recognised time and again by the Courts. In *A. L. Underwood, Ltd.* v. *Barclays Bank Ltd.*, [1924] 1 K.B. 775, the bank set up the defence that they were holders for value of cheques payable to the company, which had been passed to the account of the managing director; in the Savory case, Lord Wright, in the House of Lords, said: "The appellants (Lloyds Bank) are not claiming to be holders in due course, which would raise a different issue from the issue under Section 82."

Collecting Banker as Holder for Value. There are four cases where a banker handles a cheque as a holder for value.

Firstly, and obviously, where he cashes a cheque payable elsewhere to oblige a customer, in the same manner as a friend or tradesman might do. The form your customer signs in this connection should make it plain that you

are to have recourse against him, not only if the cheque is returned unpaid, but also if subsequently lack of title—owing to a forgery, for example—compels you to reimburse the true owner.

Of course, your customer's endorsement serves the same purpose, but if this were not on the cheque you might have trouble, at a later date, in the absence of any other admission of liability, in making him realise that as a transferor by delivery he warranted to you the genuineness of the cheque in respect of signatures thereon, and could be sued by you for breach of such warranty—see Section 58 (3)—although he could not be sued on the cheque in the absence of his signature thereon—see Section 23.

Secondly, where a customer pays in a cheque and you agree expressly or impliedly to let him draw against it forthwith before it is cleared, you collect the cheque for yourself and not for your customer. This does not cover the casual case where you pay against uncleared effects, where you know your customer to be good for the risk involved; there must be some arrangement with him that he shall be allowed to draw right away.

In *A. L. Underwood, Ltd.* v. *Barclays Bank*, *supra*, where the bank set up the defence of holders for value, because in a similar action the Bank of Liverpool pleaded the protection of Section 82, but were held to have been negligent, Lord Justice Scrutton said: "The cases where an agent for collection becomes a holder for value must turn on an express or implied agreement between bank and customer that the latter may draw against the cheques before they are cleared."

Lord Atkin was to the same effect: "To constitute value there must be a contract between banker and customer that the bank will, before receipt of the proceeds, honour cheques of the customer drawn against the cheques."

In *Lloyds Bank* v. *Hornby*, reported in *The Financial Times* of 5th July, 1933, the bank opened an account with

a cheque for £250, against which the new customer was allowed to draw. The drawer of the cheque stopped payment of it and the bank as a holder in due course sued him for the amount advanced.

The drawer sought to bring in Section 82, alleging negligence against the bank in that the account was opened without a proper introduction. The Judge held that the point was immaterial (although, in fact, there had been no negligence), as the bank was a holder for value and Section 82, therefore, had nothing to do with the case.

There are two points of interest to note here. Even if the bank had acted negligently, it would still have succeeded, provided the negligence did not amount to bad faith, for it is not a condition of a holder in due course that he shall act without negligence. Further, if the drawer had taken the precaution, mentioned in the previous chapter, of crossing the cheque "not negotiable," the bank would only have had the same title as the new account-holder, which presumably was a defective one, and hence could not have succeeded against the drawer.

Thirdly, if a customer pays in a cheque in specific reduction of an advance—not in the ordinary course of business on an overdrawn account—you are not collecting for the customer, but for yourself. You have been paid a debt by means of a cheque—it is yours and not the customer's.

Lastly, by the Bills of Exchange Act, Section 27 (2), it is laid down that "where the holder of a bill has a lien on it . . . he is deemed to be a holder for value to the extent of the sum for which he has a lien."

For example, if a cheque originally received by you as an agent for collection for your customer's credit is returned unpaid, and the state of your customer's account will not permit debiting such cheque thereto without creating an overdraft, you have a lien on the

cheque—it comes into your hands in the ordinary course of business as a banker; according to the above section you are endowed with the rights of a holder for value of the cheque, which should be debited to a suspense account. If this is done, and provided you give all necessary parties notice of dishonour, you can sue on the cheque in your own name as a holder for value.

In all these cases where you can show that you gave value for a cheque in good faith, you will be able to resist a claim by the true owner provided that the cheque is not tainted with forgery, that you had no notice of any previous dishonour or of any defect in the title of your customer—direct notice, not that indecisive kind known as constructive notice—that the cheque was not crossed "not negotiable," was not overdue for the purposes of negotiation, and was otherwise regular on the face of it in all respects. If it were so crossed, or so overdue, you would be dealing with an instrument possessing none of the qualities of negotiability and hence you would be accountable to the true owner.

Banker as Collecting Agent and his Duty to his Customer. We can now proceed to examine the position of the banker as a collecting agent pure and simple.

Firstly, as regards the customer for whom he collects cheques, he must act with due care and diligence in presenting the articles for payment, and neglect to use the customary and recognised channels may involve him in liability to his customer if the latter suffers loss.

In *Forman* v. *Bank of England* (1902), 18 T.L.R. 339, a customer paid in a cheque for £500 drawn on a Norwich bank, alternatively payable in London—the sort of cheque you occasionally meet with. The Bank of England passed this cheque through the Country Clearing and dishonoured on the following day a cheque of their customer drawn in reliance on the clearance of the cheque for £500. Evidence was called showing that it was banking custom to pass cheques so drawn through the Town

Clearing, and damages were accordingly awarded to the customer.

If any cheques presented for payment on behalf of a customer are returned unpaid, the collecting banker must give his customer due notice of dishonour, in accordance with the rules laid down on this matter in Section 49 of the Bills of Exchange Act, 1882. If such notice is not given, the customer can successfully object to being debited with the unpaid article.

Where cheques are returned to a collecting banker for confirmation of endorsement, or other cause to which he can attend without troubling his customer, notice of dishonour should, nevertheless, be duly sent to the latter. If this were not done and the cheque on representation comes back a second time with a more ominous marking for example, the customer could rightly say that, not having received notice of dishonour in the first instance, he was entitled to treat the cheque as paid.

Where a customer pays in a cheque drawn on the same bank and branch, the banker can legally hold it over until the close of business on the following day. This would in most cases be an arbitrary proceeding, and in practice such cheques are paid or returned by the close of business on the day of payment in. Of course, if the customer at the time of tendering such a cheque for his credit, asks for and is given a decisive and affirmative answer, the cheque will have to be treated as paid.

Collecting Banker's Duty to Third Parties. So much for the collecting banker's duty towards his customer. What of his responsibility towards third parties? Such responsibility arises out of the legal doctrine of conversion and all its implications.

Conversion has been defined as follows—

"Any person who, however innocently, obtains possession of goods the property of another who has fraudulently been deprived of the possession of them and disposes of

them, whether for his own benefit or that of another person, is guilty of a conversion."

It is wrongful interference with another person's property, inconsistent with the owner's right of possession. It is no defence to say that there was no intent to deprive the rightful owner of dominion over his goods, or that you were merely acting in all innocence as an agent for another party.

Now, if you apply this doctrine to the banker acting as a collecting agent, it follows that every time he handles a stolen cheque for his customer, a cheque to which the latter has no right, he is guilty of conversion. In the *Savory* case, Lord Wright said: "It was also conceded by the appellants (Lloyds Bank) that what they did constituted a conversion by them of the cheques for which the appellants in the absence of special defences were liable in damages."

The damages for conversion of a negotiable instrument are its face value, and you will perceive that, if every time you collected a stolen cheque for your customer, you were to be liable for such conversion, the collection of cheques would be a costly part of your business. In like manner as the Legislature recognised that a paying banker requires some protection from liability in paying cheques with forged endorsements, so has it admitted in Section 82 of the Bills of Exchange Act, 1882, that a collecting banker is entitled to some consideration when he converts a cheque paid in for collection.

You should realise, firstly, that Section 82 does not say that in certain circumstances a bank shall not be guilty of conversion, but that he shall not be liable for such a tort; secondly, the protection is, as we shall see, severely restricted and conditioned.

In view of the judgments based on interpretations of Section 82, judgments which often appear to bear hardly on the banker, there is an idea among some bank people that Section 82 is a sort of perpetual bugbear to a collecting

banker, an irksome restriction placed on his banking activities. As a matter of fact, the reverse is the case. It is a concession, a protection, for, in the absence of Section 82, a banker would have no defence whatsoever to a claim for damages for conversion of every stolen cheque he happened to collect. As was said in the *Savory* case: "Section 82 is, therefore, not the imposition of a new burden or duty on the collecting bank, but is a concession affording him the means of avoiding a liability in conversion to which otherwise there would be no defence."

Let us see what are the conditions attaching to this protection against liability for conversion.

Reference to Section 82 will remind you that the protection is only given in respect of crossed cheques. Other types of document, like orders for payment with receipt attached, and banker's drafts and dividend warrants, are only brought within the ambit of Section 82 by other statutes or sections.

Cheques must be crossed before they come into the banker's hands. This was the interpretation of the Appeal Court in the *Gordon* case, duly confirmed by the House of Lords, and is the reason why customers are asked to cross all cheques before handing them in for collection. Do not forget that branding your crossing stamp on a cheque has no retrospective quality, and if you collect an uncrossed cheque to which your customer has no title, or a defective title, Section 82 will not avail you, even if all the other qualifying conditions have been observed.

Meaning of "Customer." Duly crossed cheques are only protected in their collection if handled for a customer. The term "customer" has had a chequered history. The word itself would suggest "custom," some sort of continuity and course of business, shutting out an isolated and first transaction with a new account-holder.

This was the notion adopted in the case of *Matthews* v. *Williams, Brown and Co* (1894), 10 T.L.R. 386, where the Divisional Court held that the word "customer" involves

use and habit and that one transaction does not make a customer. But even if you could establish some sort of continuity, if you were in the habit of collecting cheques for a party, he was not a customer unless he had an account with you.

In *Great Western Railway* v. *London and County Bank*, [1901] A.C. 414, a Poor Law overseer fraudulently obtained a cheque from the plaintiffs for the poor rate. The cheque was crossed "not negotiable" and the local branch of the defendant bank cashed it for the overseer, who had no sort of account whatever with the bank, but had been in the habit of encashing rates cheques there for several years past.

In the Court of first instance judgment was given for the bank on the ground that it was protected by Section 82, inasmuch as it received payment of the cheque in good faith and without negligence for the overseer, who was a customer within the meaning of the section.

This judgment was confirmed in the Court of Appeal, and it is a little difficult for a layman to follow the reasons for the decision, as, apart from other matters, the cheque was exchanged for cash forthwith, and the bank became a holder for value, but not a holder in due course in view of the "not negotiable" crossing.

In the House of Lords the decision was reversed. It was held that the bank, as holder for value of the cheque, could not succeed in view of the "not negotiable" crossing; Section 82 did not help, as the bank was receiving payment for itself, and in any case the overseer was not a customer. It was said on this point: "It is true that there is no definition of customer in the Act, but it is a well-known expression, and I think that there must be some sort of account, either a deposit or a current account, or some similar relation to make a man a customer of a banker."

Although one of the other Law Lords said that "it is not necessary to say that the keeping of an ordinary banking account is essential to constitute a person a

customer of a bank," and went on to suggest that the habitual receipt of cheques for collection from a person having no account with a bank, and the payment over of the proceeds after clearance, would constitute such party a customer, I imagine that in banking circles, at any rate, the term is confined to a person who keeps an account—not necessarily a current account—with a bank.

Up to 1914, then, the doctrine of a customer was this: There must be some sort of an account opened, but the initial transaction in opening it did not set up the relation of banker and customer—there had to be some measure of continuity and custom.

But, in 1914, it was held in the case of *Ladbroke* v. *Todd* (1914), 30 T.L.R. 433, that "The relation of banker and customer begins as soon as the first cheque is paid in and accepted for collection and not merely when it is paid." This view was also taken in *Commissioners of Taxation* v. *English Scottish and Australian Bank*, when Lord Dunedin said: "The word 'customer' signifies a relationship in which duration is not of the essence."

So directly you open an account and accept the cheque for collection the relationship of banker and customer is set up. But remember that the device of opening a short account or crediting an item to "sundry persons" account will not give you protection by investing the party for whom you are collecting with the status of a customer.

In the appeal hearing of the *Savory* case, a new issue was raised by Lord Justice Lawrence. He expressed doubt as to whether an account holder paying in at one branch for the credit of his account at another branch was a customer within the meaning of Section 82. Fortunately, this was not part of the binding judgment, but rather an *obiter dictum*—something said by the way—and the fact that the House of Lords ignored the point suggests that it was not taken seriously.

We have seen then that the preliminary conditions for protection under Section 82 are, that the article collected

must be a crossed cheque and that the party for whom it is collected must be a customer.

These matters do not give a banker great concern; after all, there is some finality about the terms in question, and while there is no statutory definition of a customer, it is possible to piece together a fairly comprehensive and workable conception of the term from decided cases.

But when we come to consider the next protective element in Section 82—acting without negligence—we find that not only is there no statutory guidance as to what constitutes negligence, but that we cannot deduce from the leading cases a working definition which will serve once for all as a guide to our footsteps.

Negligence within Section 82. The legal history of negligence in relation to Section 82 reveals a doctrine that is ever shifting in its implications, that is ever expanding in its scope as new circumstances arise, so that you cannot be certain, if you are concerned with the collection of a stolen cheque in circumstances that have never been examined by the Courts before, that you will not find your conduct branded as negligent.

Inasmuch as a banker ordinarily is only under a duty to his own customer, it might be thought that he cannot be charged with negligence to the true owner—a total stranger—in view of the legal maxim that there can be no negligence unless there is a duty to be careful.

The answer is that the duty is purely a statutory one imposed on the banker by Section 82 in favour of the true owner. "There is no duty at common law on the collecting banker to exercise care; the duty is entirely created by the Act" (*Lloyds Bank* v. *Chartered Bank of India*, [1929] 1 K.B. 40).

There have been judicial expositions of the term "negligence," but of necessity they are couched in wide terms, and can hardly be regarded as working principles.

For example, in *W. Wallbank and Co., Ltd.* v. *Westminster Bank, Ltd.* (1924), the term was defined as

follows: "Negligence is the doing of that which a reasonable man, under all the circumstances of the particular case in which he is acting, would not do, or the failure to do something which a reasonable man under those circumstances would do."

Again, it has been said that "the test of negligence is whether the transaction of paying in any given cheque, coupled with antecedent and present circumstances, was so out of the ordinary course that it ought to have aroused doubts in the banker's mind and caused him to make inquiry."

You will see from this dictum that the essence of negligence is not necessarily the collection of the cheque, but the absence of inquiry where it is reasonably called for. In *A. L. Underwood, Ltd.* v. *Bank of Liverpool and Martins Ltd.* (1924), 40 T.L.R. 302, stress was laid on the fact that the managing director of the company might conceivably have been acting in the interests of the company in placing cheques payable to it to his private account, but no inquiries as to the propriety of his conduct were made, and this neglect was fatal to the bank's case.

Here is a case where inquiries were in fact made where the circumstances were suspicious but the Court held that such inquiries were not sufficiently thorough. In *Motor Traders Guarantee Corporation Ltd.* v. *Midland Bank Ltd.*, [1937] 4 All E.R. 90, a motor trader paid into his account a crossed cheque drawn by the plaintiffs payable to W. & Co. The cashier queried the transaction but was given a plausible explanation and accepted the cheque for collection. The bank's regulations required such transactions to be dealt with by the manager and not by a cashier, which was not done in this case. The customer's banking history was not good—many of his cheques having been dishonoured. It was held that a breach of the bank's regulations was not conclusive proof that insufficient inquiry had been made but that, in view of the customer's past history, the bank should have made

further inquiry. Judgment was accordingly given for the plaintiffs.

In *Slingsby and Others* v. *Westminster Bank Ltd.*, [1931] 1 K.B. 173, one of the cases concerned the collection of an interest warrant payable to "M. E. Slingsby A/c H. Turner dec'd." for the private account of the solicitor to the estate. The manager made inquires as to the transaction, and it was explained to him that the warrant was being utilised in repayment of an advance made by the solicitor to Mrs. Slingsby in anticipation of this interest payment.

The judge said: "The question was whether a reasonably competent and careful bank official would have been satisfied with the answers he received or would have pursued the matter further." He considered that satisfactory answers were received, and quoted with approval the dictum of another judge, that bank officials could not be expected to act as amateur detectives.

It is possible, despite the absence of a definition of "without negligence," to establish certain propositions as a result of decided cases that will serve as some sort of practical guide in the collection of cheques.

Firstly, it is negligence to collect a cheque on which there is an irregular endorsement. The arrangement made at branches for ensuring that all cheques remitted for collection are properly endorsed are not only designed to avoid the labour involved in the return of cheques for irregular endorsements, but also to ensure that the protection of Section 82 is not forfeited on account of failure to detect an irregular endorsement.

In *Bavins Junr. and Sims* v. *London and South Western Bank*, [1900] 1 Q.B. 270, a conditional form of cheque was collected for a thief and the endorsement thereon was irregular. The Court of Appeal held that the bank had been guilty of negligence in not detecting that the endorsement and receipt were in a different name from that of the payee.

New Customers. Secondly, omission to establish the *bona fides* of an account holder, to take reasonable precautions to ensure that you are dealing with a reputable person, will be accounted to you as negligence.

There is a whole string of decided cases on this point, and, apart from the desirability of knowing something about the man to whom you propose to entrust a cheque book, all banks to-day make it a rule, to which there is no exception, to require a satisfactory introduction or a reliable reference for all persons proposing to open current accounts; otherwise there will be no help from Section 82 if the customer passes through his account cheques to which he has no title.

In the case of *Ladbroke* v. *Todd* (1914), 30 T.L.R. 433, the John Bull Bank opened an account with a person who had stolen from a letter-box a cheque drawn by a bookmaker to settle a client's winnings. The thief was not introduced, nor did the bank ask for any references. The cheque was paid in to open the account, quick clearance was requested and obtained, followed by withdrawal of the money and disappearance of the thief.

The drawer took an assignment of his client's—the payee's—rights in the cheque and sued the bank, which was held to have been negligent in not taking reasonable precautions to safeguard the interest of persons who might be the true owners of the cheque—in other words in opening an account with a total stranger.

This was a case of total lack of introduction and there are others equally fatal to bankers, where references have been given but have not been properly verified. If a new account holder gives you the name of a total stranger as referee, you have not done all that should be done unless you take steps to find out if the referee is a fit and proper person to vouch for your new customer's respectability. It is a tedious and sometimes an awkward matter duly to prosecute these inquiries, but if you omit to do so it is at the risk of being held to have been negligent.

In *Guardians of St. John's Hampstead* v. *Barclays Bank Ltd.* (1923), 39 T.L.R. 229, a party opened a current account and was asked for a reference as he was unknown to the bank. He gave the name of a total stranger, and the reply from this gentleman as to the new customer's suitability as an account holder was eminently satisfactory—and, not unnaturally, for the customer had concocted and forged his own reference. No steps were taken to check the reference given, and this was one of the counts on which the bank was held to have been negligent.

An earlier case (*Harding* v. *London Joint Stock Bank, Ltd.* (1914)) concerned a new account-holder who was introduced by another customer of the bank. He opened an account with a cheque payable to his employer, which he had stolen. He was asked to get written confirmation of his right to deal with the cheque, which he duly furnished, having forged the authority in question himself. It was held that further inquiry was necessary as the alleged authority indicated that the new customer was an employee of the payee, and the bank had to pay.

Incidentally, banking evidence was given to the effect that where an account was opened with a cheque payable to a third party, confirmation by such party was usually obtained, notwithstanding that the new customer was personally introduced.

No one will cavil, I imagine, at the insistence of the Courts that the true owner of a stolen cheque is not to be deprived of his remedy against the bank who collected it, if the latter has not troubled to satisfy himself that the party who paid it in is a respectable and reputable person. The *Savory* case, however, has stretched this doctrine considerably further in two directions.

The House of Lords in that case confirmed that if you know a man is an employee you must, under pain of being held negligent, ascertain who is his employer, in order that you shall be in a position to challenge any dealings by the customer with his employer's cheques. Until

this decision, a banker had, as a matter of expediency, endeavoured to get hold of this and any other relevant information for his private records; where possible, a reference from the new customer's employers would be suggested, but there had been no recognition of any duty in this connection.

The essence of the *Savory* case was that a stockbroker's clerk, known to be such and introduced by another customer, paid in to his account cheques drawn by his firm which he had stolen. The bank were aware of his occupation, but ignorant of his employers.

Lord Wright said of this feature: "Where the new customer is employed in some position which involves his handling and having the opportunity of stealing his employer's cheques, bankers fail to take adequate precautions if they do not ask the name of his employers; this is especially true of a stockbroker's clerk; it may be different in the case of an employee whose work does not involve such opportunities, as, for instance, a technical employee in a factory."

He went on to distinguish between information as to a customer's respectability and standing, and information as to his employers. "A reference or introduction merely speaks to the general reputation of the man; knowledge of who are his employers is aimed at an entirely different purpose—that is, to arm the bank against a known even if problematical risk; it is, unfortunately, common knowledge that persons of respectability, well introduced, may still commit fraud."

In the earlier case of *Lloyds Bank* v. *Chartered Bank of India*, [1929] 1 K.B. 40, the same point had been made—"It is very important to maintain safeguards against employees dealing with their masters' property without authority."

Whatever we may think of the reasonableness of these new requirements, we must understand that, as the law now stands, ignorance as to a customer's employers will

be a bar to protection under Section 82 if cheques drawn by or payable to such employers are collected for the customer in circumstances where he has no title to them. Presumably this will mean keeping track on a customer's change of employer.

Then a more startling rule, and one likely to lead to trouble, was enunciated in the *Savory* case in connection with the frauds perpetrated by the second stockbroker's clerk. This party used his wife's account for collecting cheques drawn by his employers. The bank knew nothing of the lady's husband or his occupation, and the finding of the Court of Appeal was confirmed—namely, that it was negligence on the bank's part not to have made inquiries as to the occupation and employer, if any, of the lady customer's husband, inasmuch as the affairs of husband and wife are usually mutual. In fact, Lord Justice Scrutton, in the Appeal Court, said that if there was no need to inquire about the husband, accounts in the names of the wives of dishonest clerks would become as popular as they appear to be in the case of fraudulent bankrupts.

I can imagine cases where inquiries of a salaried man, about to open an account, concerning his employers might provoke discord at the initial stages of banking relationship; much more, therefore, can I visualise trouble and the possible loss of a potentially valuable account if a married woman is to be catechised as to her husband's mode of livelihood and the people who provide him with his bread and butter.

Possibly a manager trained in watching customers' reactions to leading questions might postpone the piquant situation until such time as the husband or wife paid in third party cheques. In such a case failure to inquire would place you right outside the pale of Section 82.

One further cautionary word before we leave the subject of references. If a deposit, or indeed a home safe account, is used for the purpose of the collection of cheques, or if

a depositor subsequently opens a current account, circumstances may demand the making of inquiries as to his respectability as in the case of a new customer opening a current account. The fact that it is not customary to ask for an introduction or references in the case of a deposit account will not excuse such formality in the above circumstances.

Thirdly, the collection of cheques payable to third parties may, *in certain circumstances*, prevent you from getting protection under Section 82 on the grounds of negligence. First of all, let me stress the fact that there is nothing statutory or otherwise that says that crediting a cheque payable to "A" to "B's" account is a matter that calls for inquiry, and to suggest otherwise is to strike at the very roots of negotiability. Furthermore, a cheque payable to "A" and crossed "Not negotiable" may safely be collected for "B's" account, provided you are not aware of any fiduciary relationship between the two parties. The words "Not negotiable" are addressed neither to the paying nor collecting banker as such, but, as I have mentioned before, constitute a warning to any one who proposes to take the cheque as a holder.

But there are certain cases where the crediting of third party cheques is fraught with risk. For example, where a cheque is crossed "A/c payee" or "A/c X.Y." there is a clear indication that the drawer or the payee has designated a particular account to which the cheque shall be credited. Such additions to a crossing find no mention in the Bills of Exchange Act, yet disregard of such markings may involve you in liability simply and solely on the grounds of negligence. It matters not if the cheque is payable to order or to bearer—the addition to the crossing must not be ignored by the collecting banker (*House Property Company of London, Ltd.* v. *London County and Westminster Bank, Ltd.* (1915), 31 T.L.R. 479).

Again, if an employee places a cheque payable to his employer to his private account, or if an official of a

company likewise deals with a cheque payable to a company, or if an agent similarly uses a cheque payable to his principal, a bank will get no relief from liability if the employee, the official, or the agent has in fact misappropriated the cheque, and the bank knew, or should have known, of the fiduciary capacity in which its customer stood.

Collection of Cheques Payable to Company. The decided cases which go to demonstrate this liability form a melancholy tale, and perhaps the most frequent example is the director of the so-called "one-man" company, who wilfully or in ignorance of the essential distinction between himself and the separate entity, the company, puts to his own account cheques payable to the latter.

The cases of *A. L. Underwood, Ltd.* v. *Bank of Liverpool and Martins, Ltd. and the same* v. *Barclays Bank, Ltd.*, [1924] 1 K.B. 775, to be found in the third volume of *Legal Decisions Affecting Bankers*, may be read with profit in this connection.

It may be asked: is a bank put on inquiry where a cheque payable to a limited company, and duly endorsed by it, is tendered for the credit of another account, either of an individual or a company? I mentioned just now that a cheque payable to "A" may safely be collected for "B," but where the payee is a limited company a practice has grown up of querying such a transaction.

Strictly speaking, there appears to be no good reason for drawing such a distinction, save that limited companies usually find a home for all cheques payable to them in their own accounts.

In *London and Montrose Shipbuilding Company, Ltd.* v. *Barclays Bank, Ltd.* (1926), 31 Com. Cas., it was held in the lower Court that a company's cheque could be placed to the account of a third party without risk in the absence of circumstances that would indicate fraud, and the judge held that to draw the above-mentioned

distinction between an individual and a limited company, with the attendant necessity for inquiry, was putting the matter impossibly high. It is true that the verdict in favour of the bank was reversed on appeal, but this was presumably because the cheque payable to the plaintiff company was paid into the account of another company, with which the director of the first company was closely connected.

But "the only prudent course is for bankers to refuse to accept without inquiry or special instructions cheques made payable to companies for accounts other than those of the payee"—this was the view of Mr. Goddard, K.C. (now Lord Goddard, C.J.), based on the fact that "in *Savory* v. *Lloyds Bank*, ... all the banking witnesses stated that it was now the recognised practice to refuse acceptance of a cheque payable to a limited company for the credit of an individual's account without inquiry," and that this "is now proved to be the practice of bankers."

In like manner it will be negligence on the part of a bank to place cheques payable to a firm to the private account of one of the partners in the firm, without prosecuting inquiries and getting a reasonable answer as to the regularity of the transaction.

Collection of Cheques drawn by Company. Then there is a further type of questionable transaction, not always so easy to detect—where third party cheques, *drawn* by an employer, a company, or a principal, are paid into an account of an employee, an official, or an agent. All such cases cry out for inquiry and you abstain from such inquiry at your peril.

The case of *Souchette, Ltd.* v. *London County Westminster and Parr's Bank, Ltd.* (1920), 36 T.L.R. 195, is illustrative of this point. Here a customer, who was managing director and secretary of a limited company, paid into his private account cheques drawn by the company payable to the order of one of its creditors. The bank knew of the relationship in which their customer

stood to the company, but made no inquiries as to why cheques of this description, payable to a third party, were being thus used, and were held to have been negligent.

Those of you who may read this case in the third volume of *Legal Decisions* will find that the Court drew a sharp distinction between such "order" cheques and cheques payable to the same payee or bearer. It was suggested that this latter type of cheque might have been drawn by the company for book-keeping convenience, but I submit that in such a case the cheques should have been paid into the company's own account, as is done frequently with wages cheques—cash having been taken out of the company's cash box and the cheque substituted.

The *Savory* case, to which I have had so often to refer, is a similar example of the wrongful use by an employee of a principal of cheques drawn by such principal payable to a third party, and you should remember that this was the essence of the case against the bank—the dealing with an employee who was misappropriating his employer's cheques. There were incidental matters, such as the bank's lack of knowledge of its fraudulent customer's occupation, already referred to, and the matter of the branch credit system, to which I shall refer presently.

In *Carpenters Company* v. *British Mutual Banking Co. Ltd.* (1937), 53 T.L.R. 276, the bank was acting both as collecting and paying banker. The plaintiff's secretary paid into his account at the defendant bank cheques drawn by his employers on the same banking office and payable in some cases to sundry creditors of the company and in other cases to fictitious persons. An action for conversion was brought by the plaintiffs and the defendant bank pleaded that the cheques had been duly paid and were covered by the relevant sections of the Bills of Exchange Act 1882 and the Stamp Act 1853. In addition to setting up as paying bankers duly protected by the Bills of Exchange Act, the defendants claimed as collecting

bankers the protection of Section 82 of the same Act. In the Court of First Instance, judgment was given for the defendant bank on the footing that it had paid the cheques in due course being protected by Section 60. It was held that the bank's negligence did not mean that it had not acted in the ordinary course of business. On appeal, however, the decision was reversed and it was held that the bank had converted the cheques in its capacity as collecting agent and, having acted negligently, was not entitled to the protection of Section 82. The protection of Section 60 in its function as paying banker did not relieve the defendant bank from liability as collecting agent. It was also held that the Stamp Act, 1853, is impliedly repealed by Section 60 of the Bills of Exchange Act.

Then, occasionally, the question crops up of a cheque drawn by a partner in a firm, in accordance with authority given, payable to himself, being paid in to such partner's private account. According to the decision in *Backhouse* v. *Charlton* such a transaction need not excite suspicion, possibly on the ground that it may well represent repayment of a loan to the firm, or a share of partnership profits. I suggest, however, that the amount of the cheque and knowledge of the partner concerned would influence a banker in his attitude towards such a transaction.

But there is one case which would cry aloud for inquiry—where a partner pays into his overdrawn account such a cheque, as a result of pressure on the bank's part for liquidation of his indebtedness.

Abnormal Operations on an Account. Fourthly, operations of an abnormal character on an account of a kind that should reasonably provoke comment, will be regarded as evidence of negligence if they pass unnoticed. You will notice that this is getting away from the idea of negligence in connection with a particular cheque and is spreading the banker's risk over the whole course of the account.

I do not recall any one case which was decided against

a bank solely on this ground, but in several instances it has been a feature sufficiently marked to come under judicial notice in the shape of an analysis of an account as regards the amount of the several cheques collected and the period of time over which they were collected.

Thus, in *Crumplin* v. *London Joint Stock Bank* and *Morison* v. *London County and Westminster Bank*, both to be found in Volume 3 of *Legal Decisions Affecting Bankers*, the Court considered in connection with the charge of negligence the size of the cheques paid in, increases in the amounts thereof, and the period involved. In the latter case there was a progressive increase in the sums paid into the private account of Morison's managing clerk, but Lord Reading held that such increases were consistent with a possible increase in the managing clerk's salary or commission.

In *Commissioners of Taxation* v. *English Scottish and Australian Bank*, the Privy Council saw nothing to excite comment in the opening of an account with a small sum in notes, followed by the payment in next day of a large cheque; in *Guardians of St. John, Hampstead* v. *Barclays Bank, Ltd.*, however, the same feature of the opening of an account with a small sum one day and the lodgment of a large cheque for collection the next day was one of the incidents which led the Court to find negligence against the bank.

Sir John Paget seems to incline to the view taken in the latter case, but in practice it is quite conceivable that a new customer would open an account with a nominal sum, explaining that a big cheque was following—this was what happened in the *Guardians* case—and it is a little difficult to see anything to arouse suspicion in these circumstances alone.

I suggest that a greater danger lies in shutting one's eyes to transactions on an account incompatible with your customer's known circumstances in life. An inflated credit turnover on a clerk's account, for instance, or on

the account of a man known to be in a small way of business, is a matter for judicious inquiry. This is one of the reasons why a branch manager, or a senior official, likes to scrutinise periodically cheques paid in for collection.

In *Lloyds Bank, Ltd.* v. *Chartered Bank of India*, [1929] 1 K.B. 40, a clerk of the plaintiff bank fed his account at the defendant bank with bank drafts drawn in fraud of Lloyds Bank, immediately drawing the money out by payments to stockbrokers. It was held that the absence of inquiry as to the source of such large amounts—sums incompatible with salary—coupled with the fact that the account was generally in low water, was negligence on the part of the Chartered Bank.

In the *Savory* case, in the Court of Appeal, Lord Justice Scrutton significantly hinted that there was a further element of negligence in the lack of inquiry as to the size of the operations on the account. He said: "The nature of the account seems to me suspicious. Perkins they knew to be a stockbroker's clerk. Into his account were paid once, twice, or thrice a month sums considerable for the size of the account, amounting in one year to over £1000."

While there is nothing to suggest that failure to query abnormal operations on an account will in itself fix a bank with negligence, it is very probable that any such laxity will be a contributory feature in any conversion action.

Lastly, it is no good to plead exigencies of business in excuse when faced with a charge of negligence.

In *Crumplin* v. *London Joint Stock Bank, Ltd.* (1913), the novel plea was raised that the cheques in dispute did not come under the manager's notice, and that the clerks who handled them could not be expected to know all about the Bills of Exchange Act. Possibly this was in the days before head office circulars and the activities of the Institute of Bankers had remedied any disparity

in knowledge between managers on the one hand and mere cashiers on the other, but at any rate the plea found no favour with the Court. The judicial attitude has always been that, if you set out to do banking business, you must employ competent officers and devise an adequate system for the efficient conduct of such business.

In this connection the attitude of the Courts in the *Savory* case towards the branch credit system is illuminating. You will remember that in this case the cheques concerned were paid in at a City office for the credit of accounts in the country. The City office was aware that the cheques paid in were drawn by a firm of stockbrokers, but were unaware that they were going to the account of a stockbroker's clerk.

The country branches which received the credits knew that the cheques were going to the account of a stockbroker's clerk, but did not know that the credits comprised cheques drawn by a stockbroking firm. All the information necessary to nip the fraud in the bud was in the bank's hands, but it was so divided as to be entirely useless.

The Court, however, refused to consider these circumstances as mitigating, and dealt with the case as if the cheques were paid in at the branch where the account was kept. "The appellants' liability must be determined altogether apart from the working of their system. From that system as such, in its every detail their own handiwork, they can claim no protection whatever."

Consequently, arrangements are now in force whereby third party cheques paid in under the branch credit system are passed on to the branch where the account is kept in all cases where the receiving branch is not entirely satisfied as to the *bona fides* of the transaction.

Contributory Negligence as a Defence. In conclusion, there is little hope of relief in the direction of contributory negligence, or in pleading that you were lulled to sleep by the true owner's conduct. In *Morison* v. *London*

County and Westminster Bank, Ltd., the bank succeeded in the case of certain converted cheques, not on the ground that Morison was guilty of contributory negligence in failing to detect his managing clerk's irregularities, but on the ground of ratification in that he knew of the defalcations but was content to forgive the delinquent and continue him in his employment. The circumstances here were so peculiar, however, that the doctrine of ratification hardly enters into our consideration.

The true owner of a cheque may facilitate its theft and conversion by his lack of care, but the duty of the collecting banker towards the true owner is not reciprocal as it is between the drawee banker and the drawer. The true owner cannot have contributory negligence alleged against him by a collecting banker, for negligence implies a duty and neglect thereof, and the true owner owes no duty to the banker. Conversely, the true owner *can* allege negligence against the collecting banker, for the latter is under a duty—a statutory one thrust on him by Section 82—to be careful in handling other people's cheques.

Analogous Instruments. A banker in these days has the job of collecting a variety of instruments in addition to cheques, and his protection from liability for conversion in so doing depends on the class of article he is dealing with.

Banker's drafts can now be regarded for the purposes of collection exactly like cheques, for the Bills of Exchange Act (1882) Amendment Act, 1932, provides that Sections 76-82 of the principal Act shall apply to such instruments.

Orders on a banker with receipt attached, referred to in an earlier chapter, and warrants on the Paymaster General are, by Section 17 of the Revenue Act, 1883, brought within the scope of the crossed cheque sections of the Bills of Exchange Act, 1882; but, as far as I can see, the only purpose such provision serves is to protect you against collecting them for a party who has forged the payee's signature and is holding himself out to be the

payee. If they bear evidence of transfer—for example, if you collect for anyone other than the ostensible payee—you are without protection.

Then orders on other Government Departments and Post Office money orders are frequently paid in for collection. There is no protection in dealing with such documents, and hence you should not be without knowledge of the person tendering them for collection.

Dividend warrants are brought within the protection of Section 82 by Section 95 of the Bills of Exchange Act, 1882, but interest warrants are presumably outside the pale if not in the form of a cheque, and no protection can be got from any statute in respect of these documents. There would appear to be one exception—warrants drawn on the Bank of England for interest on Government stocks.

In the first of the *Slingsby* cases against Westminster Bank Ltd. it was held that under the National Debt Act, 1870, the term "dividend" was used throughout in respect of interest on Government stock, and Section 95 of the Bills of Exchange Act, 1882, when speaking of a dividend warrant, included warrants of this description.

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